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No. 85- 36

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

MICHAEL CEASAR,

Petitioner,

-against-

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTIONS PRESENTED

1. Whether plaintiff's complaint pleaded fraud with particularity sufficient to: (i) satisfy the pleading requirements of F.R.C.P. 9(b); and (ii) defeat defendants' motion to dismiss converted into a motion for summary judgment, where the rigid pleading requirements of the case relied on by the Second Circuit in terming this case "fraud by hindsight" are not followed by other Circuits and have been disavowed by scholarly writers.

2. Whether the Circuit Court erred in affirming the District Court's grant of summary judgment at the pleading stage of a securities fraud action where: (i) the pleadings, and documents sought to be presented, raised genuine issues of material fact concerning

defendants' conduct; (ii) the facts concerning the alleged fraud are peculiarly within the defendants' knowledge; and (iii) plaintiff was denied discovery, sought in order to oppose summary judgment.

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-against-

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner Michael Ceasar, respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this proceeding on April 8, 1985.

OPINIONS BELOW

The order of the United States District Court for the Eastern District of New York is unreported. The decision of the United States Court of Appeals for the Second Circuit, affirming said order, is unreported. The decisions of both the Second Circuit and the District Court are set forth in the Appendix (A-6-8, 20-23).

JURISDICTION

This Petition for Certiorari is filed pursuant to 28 U.S.C. § 1254(1). Federal jurisdiction was invoked in the United States District Court under Section 27 of the Securities Exchange Act of 1934 (the "Act") (15 U.S.C. § 78aa), as amended. The order of the District Court granting summary judgment to defendants was timely appealed to the

Second Circuit. The Second Circuit affirmed on April 8, 1985.

STATUTORY PROVISIONS INVOLVED

Involved in this case are Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j(b)), Rule 10b-5 of the Securities and Exchange Commission (17 CFR 240. 10b-5), Rules 1, 8, 9(b), 12, 16, 26, 56 and 60(b) of the Federal Rules of Civil Procedure ("F.R.C.P.") and the Rules Enabling Act. These are set forth in the Appendix (A-208-216).

STATEMENT OF THE CASE

This action was brought to enforce defendants' liability for misconduct created by Section 10(b) of the Act and Rule 10b-5, promulgated thereunder. It is based upon alleged wrongdoing concerning Merrill Lynch & Co., Inc.'s

("Merrill Lynch") published financial statements for the first and second quarters of 1983. These publicly disseminated and filed documents were silent as to Merrill Lynch's exposure for huge losses as a result of its substantial sales of Baldwin United Corporation's ("Baldwin") single premium deferred annuities ("SPDAs") and its status as a large creditor of Baldwin.

Plaintiff purchased 100 shares of Merrill Lynch on July 5, 1983, 100 shares on July 28, 1983 and 150 shares on September 13, 1983 (A-30). Said purchases were made at prices artificially inflated by the defendants as a result of false or misleading statements in, or material omissions from, Merrill Lynch's first two 1983 quarterly financial reports disseminated to shareholders and the financial community. The first

purchase was made after dissemination of the 1983 first quarter report, which claimed record earnings (A-59-60) and, after announcement of glowing prospects for the future (A-38). Plaintiff's additional purchases were made while he was a stockholder and after the issuance of the second quarter report, which claimed record earnings for the second quarter and first half of 1983, resulting from a "generally very strong showing in the great majority of our activities." (A-60-62).

The facts set forth in the complaint* disclose that prior to plaintiff's purchases, Merrill Lynch was "intimately familiar with the financial condition of

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* All references to the complaint refer to the amended complaint, which was filed as a matter of right, and is set forth in the Appendix without exhibits.

Baldwin and its subsidiaries" (A-42) through the sale it made to Baldwin of AMIC Corp. (A-42) and its participation in the MGIC Corp. sale to Baldwin (A-44). As a result of the AMIC sale, Merrill Lynch became a creditor and holder of approximately $90 million in notes of Baldwin and monitored its deteriorating financial condition (A-43).

The complaint further set forth such evidentiary allegations as that Baldwin had purchased MGIC Investment Corp. for $1.2 billion and arranged bank loans of over $.5 billion in order to pay for such purchase (A-44); that in 1982, Baldwin, to the knowledge of Merrill Lynch, was unable to meet the targeted payment dates it established for such purchase; and that Merrill Lynch participated in and aided in such acquisition which it thereafter moni-

tored (A-44-45). The complaint further alleged that Baldwin subsidiaries were paying higher interest to SPDA holders during the period 1979-1983 than Baldwin was earning on its investments, thus losing money on each SPDA sale (A-46-48); that Merrill Lynch disregarded special reports available to it, but not to plaintiff, which "specifically described the illiquidity and problems" of Baldwin (A-51); that Merrill Lynch violated state statutes and regulatory requirements and federal law (A-51-52); that various state regulatory authorities began investigations which resulted in remedial orders and limitations (A-50-52); and that Merrill Lynch was selling unregistered securities of Baldwin (A-36-37, 51-52).

The complaint particularized facts such as that Merrill Lynch failed to disclose the adverse impact Baldwin's

increasingly poor financial condition would have upon Merrill Lynch's financials (A-62-64); that Baldwin was unable to meet the payments owed to Merrill Lynch under the terms of the AMIC sale (A-41-43, 62-63); that, prior to September 1982, the State of Texas had refused to allow Baldwin to register securities because of the inability of Baldwin to meet its debt obligations (A-50); that Merrill Lynch's sales tools which it used in selling Baldwin SPDAs were misleading (A-53); and the reasons therefor (A-54-56).

The comlaint sets forth the bases for Merrill Lynch's knowledge of the facts alleged with such great particularity in the complaint or for its reckless disregard of such facts, noting that by reason of its being a substantial and continuing creditor of Baldwin and by virtue of its superior research and

analysis activities concerning the financial difficulties of Baldwin and Baldwin's inability to meet its obligations Merrill Lynch knew or should have known of the foregoing facts (A-56-57). Finally, the financial difficulties Baldwin faced, as disclosed by regulatory proceedings concerning six of its subsidiaries and the actions taken by certain regulatory authorities, alleged to have been known by Merrill Lynch, were factually set forth in detail in the complaint (A-56-57). Moreover, all of the allegations of the complaint were supported by the exhibits annexed thereto.

Within 10 days of plaintiff's last purchase, the Factor lawsuit against Merrill Lynch and others, brought on behalf of Baldwin SPDA purchasers, was announced. The stock price of Merrill Lynch fell (A-68). In support of his

allegation of damages suffered, plaintiff submitted the affidavit of a damage expert.

Within four months of plaintiff's last purchase, Merrill Lynch announced that it had charged off $154 million (pre-tax) against its 1983 earnings, including its reported record earnings of the first and second quarters upon which plaintiff had relied in making his successive purchases. Merrill Lynch stated that $88 million of the $154 million was charged off in order to pay persons who purchased Baldwin SPDAs from Merrill Lynch. An additional $66 million was stated to have been taken as a reserve against the debt owed by Baldwin to Merrill Lynch as a result of Merrill Lynch's direct transactions with Baldwin by which Merrill Lynch became a Baldwin creditor (A-68-69).

Both the original and consolidated amended Factor complaints were before the courts below, as was Merrill Lynch's answer* to the latter. Exhibits annexed to plaintiff's complaint confirmed that Merrill Lynch had set aside monies to recompense Baldwin SPDA purchasers to whom it had sold securities; disclosed Wall Street's startled reaction to the setting aside of "88 million as partial reimbursement for its customers who bought" Baldwin SPDAs and the observation by others that Merrill Lynch's plan to partially reimburse SPDA purchasers was "a recognition by the company [Merrill

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* Merrill Lynch originally claimed that it was unable to answer the Ceasar complaint although it had no trouble answering the Factor complaint containing similar allegations. The only major difference being that the complaints were brought on behalf of different classes each of which was injured by the same wrongs.

Lynch] that it is on shaky legal ground" and "is very concerned about its liability"; and disclosed the fact that Merrill Lynch, among other firms, by proposing partial re-payment was trying to persuade SPDA holders who had filed 51 different Federal Court lawsuits to drop them.

The record below also includes the facts that Baldwin had sold 163,000 SPDAs with a value of $4.2 billion; that SPDAs were sold to more than 40,000 people; and that Merrill Lynch was the biggest marketer of these SPDA sales. Most importantly, plaintiff presented factual evidence to the Court below that in January 1983 and prior thereto, many other large brokerage houses, including Prudential Bache, Bear Stearns & Co. and Smith Barney, Harris Upham & Co., instructed their brokers to "defer active marketing" of Baldwin SPDAs (A-52).

Merrill Lynch, however, continued to actively sell them, despite the fact that analysts and rating services had lowered their ratings on Baldwin securities partly because Baldwin had deferred the date of payment of its obligations on its MGIC investment; and despite Merrill Lynch's knowledge of Baldwin's illiquidity and other problems.

The record below also included at least fifteen (15) negative articles concerning Baldwin published between January 1983 and April 15, 1983 when Merrill Lynch, acknowledging the serious risks involved, first told its salespeople to stop selling the Baldwin SPDAs. These articles referred to stock fluctuations causing material concern among stock analysts, brokers recommending curtailing of sales of Baldwin SPDAs, restructuring of short-term debt because of inability to meet payments when due, forecasts of

Baldwin's present and future financial difficulties, lack of agreement among Baldwin creditors to extend Baldwin debt due and past due, lowered Standard & Poor's ratings on Baldwin debt, a very short extension of debt being granted by Baldwin's creditor banks for the purpose of allowing them to determine whether Baldwin's finances justified a further extension of time to pay, Baldwin's announcement of substantially lower earnings, Baldwin's requests to banks to postpone repayment while it attempted to work on a debt repayment plan, announcement by Baldwin of a 1982 fourth quarter loss of $2.8 million, net income of substantially less than in 1981 and failure to make promised payment to a creditor which raised doubt that Baldwin would be able to reschedule its short-term debt.

From the complaint and the numerous exhibits submitted below it would be an understatement to claim that there were sharply contested issues of fact as to the extent of defendants' knowledge of Baldwin's financial difficulties, as to when defendant was put on notice as to these difficulties and as to the effect of these difficulties on Merrill Lynch's announced earnings. The complaint, together with the exhibits annexed thereto, sufficiently stated a detailed claim for violation of § 10(b) and could and should have led the Court of Appeals to reverse the District Court's granting of summary judgment.

The procedural history of this action begins with the filing of the complaint on February 1, 1984, shortly after Merrill Lynch announced huge material writeoffs affecting its previously disseminated financials.

Defendants, by motion filed April 20, 1984, pursuant to Rules 9(b) and 12(b) of the F.R.C.P., moved to dismiss plaintiff's complaint for failure to plead fraud with particularity. On June 1, 1984, plaintiff filed his memorandum of law in opposition to defendants' motion. The Court, by Order dated July 27, 1984, converted defendants' motion into a motion for summary judgment (A-1-3). On August 22, 1984, plaintiff filed his amended complaint, as of right. Defendants, by amended notice of motion, moved to dismiss the amended complaint on the same grounds, for failure to plead fraud with particularity (emphasis added). Limited discovery, duly sought in order to enable plaintiff to oppose the summary judgment motion, was denied and none has been had (A-4-5). The Court, in granting summary judgment to defendants, despite the detailed factual allegations and exhibits,

and despite the sharp issues of fact raised, dismissed the complaint on October 10, 1984, characterizing it as "fraud by hindsight" and stated that to allow discovery would be equivalent to permitting a "fishing expedition" (A-6-8). Judgment was entered on October 18, 1984 (A-9-10). Plaintiff's motion for reargument or reconsideration of the stay of discovery was denied on November 9, 1984 (A-11-14).

On December 10, 1984, plaintiff filed his Notice of Appeal. In January 1985, plaintiff obtained two documents, a "Notice of Intent to Issue an Adjudicatory Order and of Respondent's Right to Hearing," issued by the State of Ohio, Department of Insurance (A-92) and the "Examiner's Statement of Investigation", issued to the Bankruptcy Court for the Southern District of Ohio, Western Divi-

sion (A-133), which came into existence wich came into existence after the District Court's dismissal of plaintiff's complaint, and after the filing of plaintiff's Notice of Appeal.

Plaintiff moved, pursuant to F.R.C.P. Rule 60(b), for Relief From Judgment or Order Based upon Newly Discovered Evidence, dated February 5, 1985. The motion was denied by the District Court on March 8, 1985 (A-15-16).

Plaintiff then sought, by motion dated March 19, 1985, to expand the record on appeal by including in the Joint Appendix the two documents referred to in the 60(b) motion, supra, as well as two additional documents which later came into existence, the Motion of the State of Maine, as Amicus Curiae, "In Opposition to Proposed Class Action Settlement" (A-149) and the "Memorandum of the Amici States in Opposition to

Proposed Class Action Settlement" (A-165), both filed in the District Court for the Southern District of New York, or, in the alternative, to have the Court of Appeals take judicial notice of these documents (A-73). Plaintiff's motion was denied on March 25, 1985 (A-17-19).

Had the court taken judicial notice of these documents, the allegations of plaintiff's complaint as to defendants' knowledge of Baldwin's grave financial difficulties, and as to defendants' own exposure at the time Merrill Lynch was claiming record profits, would have been even further buttressed (A-80-89).

One of these documents, Baldwin's "Examiner's Statement of Investigation" specifically states that Morley Thompson's (Baldwin's Chief Executive Officer) recollection of events, if substantiated "would furnish the basis for a major claim by the company [Baldwin] against

Merrill Lynch." (A-143). It further states that if certain "assumptions are correct, Merrill Lynch -- by letting objectivity yield to self-interest and by permitting itself to be used as a means of tying down financing for the acquisition [of MGIC] -- bears a share of the damage that has been done to the Debtors in these proceedings." (A-147-148).

Thus, it clearly appears that Merrill Lynch was well aware of the liability it faced.*

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* Since the dismissal of this action, the Attorneys General for the various states opposing the proposed $135 million class action settlement ($44 million to come from Merrill Lynch, the largest SPDA seller) on behalf of Baldwin SPDA holders (A-165) have appealed the District Court's approval of the settlement. The appeal to the Second Circuit was filed on or about May 31, 1985 and is pending as of the date of filing of this Petition.

Excerpts from this and the other three excluded documents, to which the Circuit Court was referred and to which this Court is respectfully referred (A-92-207), and all of the documents placed before the Courts below, reveal that at the time Merrill Lynch announced record first and second quarter earnings for 1983, it knew or should have known of at least the following: that it had engaged in deceptive practices in the sale of unregistered securities (Baldwin SPDAs); that its sales of such securities were made through materially false statements to purchasers of the SPDAs, including the description of the SPDAs by Merrill Lynch to purchasers as being safe, guaranteed and risk-free investments; that Merrill Lynch's probability of collection of Baldwin's debt to it was highly dubious in view of its awareness of

Baldwin's shaky financial resources; and that Baldwin's pending insolvency would have a drastic impact on Merrill Lynch's reported "record" earnings and future operations.

The Second Circuit affirmed the District Court and granted summary judgment to defendants on April 8, 1985 (A-20-23).

REASONS FOR GRANTING THE WRIT

1. The conflict between the Second Circuit's rigid application of the pleading requirements for fraud under Rule 9(b) as compared to requirements employed by other circuits, affords this Court an opportunity to decide a question not previously ruled upon by the court, which is the subject of division among the circuits and of intense scholarly debate.

Rule 9(b) states that all averments of fraud must be alleged with particularity (A-210). However, there is no set guideline to facilitate the determination of exactly what constitutes sufficient particularity. Hence, a split of authority, as demonstrated by the Second and Third Circuits, has evolved among the courts.

The Court below, in affirming the judgment of the district court, premised its opinion on Denny v. Barber, 576 F.2d

465 (2d Cir. 1978). The Second Circuit, in Denny, adopted a rigid interpretation of Rule 9(b) and labelled the allegations as constituting "fraud by hindsight." Denny v. Barber, supra, 576 F.2d at 470. The Court below applied this amorphous and ill-defined phrase to the instant case, as well.

The Third Circuit, has long rejected Second Circuit opinions, as espoused by Denny v. Barber, supra, and applies Rule 9(b) in a more flexible manner. The Third Circuit aptly stated in Christidis v. First Pennsylvania Mortgage Trust, 717 F.2d 96, 99 (3rd Cir. 1983), that it "finds more appropriate guidance [in 9(b) matters] . . . closer to home."*

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* The Pennsylvania District Court in interpreting Christidis stated that ". . . the Third Circuit declined to follow Decker [Decker v. Massey-Ferguson, Ltd., 681 F.2d 111 (2d

(continued on next page)

The split of authority is also reflected in many District and Circuit Court cases. These cases are closely analyzed in Note: Pleading With Particularity, 97 Harv. L. Rev. 1432 (1984) ("Harvard Note") and Sovern, Reconsidering Federal Civil Rule 9(b): Do We Need Particularized Pleading?, 104 F.R.D. 743 (1985) ("Sovern").

The great disparity between pleading requirements under 9(b) in the Second Circuit and other c.rcuits is demonstrated by cases such as Walling v. Beverly Enterprises, 476 F.2d 393, 397 (9th Cir. 1973), where the Ninth Circuit stated that while the circumstances

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* Cir. 1982)] and similar [Second] Circuit] cases, [e.g., Denny v. Barber] counseling a restrictive view of 9(b)." Thomas v. Tramiel, Fed. Sec. L. Rep. (CCH) ¶92,030 at 91,123, n.2 (E.D. Pa. April 15, 1985).

constituting fraud must be alleged with particularity, the rule does not require the pleading of detailed matters; instead, "[i]t only requires the identification of circumstances constituting fraud so that defendants can prepare an answer"; Christidis v. First Pennsylvania Mortgage Trust, 717 F.2d 96, 100 (3rd Cir. 1983) ("focusing exclusively on particular langauge is too narrow an approach and fails to take into account the general simplicity and flexibility of the rule"); Kitchens, et al. v. U.S. Shelter Corp., et al., Fed. Sec. L. Rep. (CCH) ¶91,838 (D.S.C. 1984) where the District Court, articulating the view of the 4th Circuit, stated:

> The defendants rely on authority from the Second Circuit, which has dismissed various cases on the ground of insufficient particularity. . . . The Fourth Circuit, however, has refused to adopt these stringent pleading requirements. . . . [A] motion

> to dismiss will be denied unless it appears to a certainty that no possible set of facts could be proved to support plaintiff's claim. It is clear that in this circuit Rule 9(b) must be read in light of Rule 8.

Id. at 90,200 (citations omitted); Carroll v. First National Bank of Lincolnwood, 413 F.2d 353 (7th Cir. 1969) cert. denied, 396 U.S. 1003 (1970) (rule 9(b) is not intended to abrogate basic pleading requirements of Rule 8(a)); U.S. v. Gill, 156 F. Supp. 955 (W.D. Pa. 1957) (fraud is not required to be pleaded with absolute and detailed particularity); Whittlin v. Giacalone, 154 F.2d 20 (D.C. Cir. 1946) (all that is required is that circumstances be pleaded with sufficient definiteness as to advise the adversary as to the claim he must meet); Lewis v. Berry, Fed. Sec. L. Rep. (CCH) ¶91,403, 98,014 (W.D. Wash. 1984) ("The Ninth Circuit has adopted a less

strict interpretation of Rule 9(b) than has the Second Circuit"); Zatkin v. Primuth, 551 F. Supp. 39, 42 (S.D. Cal. 1982) (exclusive focus on the fact that Rule 9(b) requires particularity in pleading "is too narrow an approach and fails to take account of the general simplicity and flexibility contemplated by the rules"). Furthermore, the Eleventh Circuit has attempted to harmonize rule 9(b) with the broader policy of the F.R.C.P., which "reject[s] the approach that pleading is a game of skill in which one misstep by counsel may be decisive to the outcome and accept the principle that the purpose of pleading is to facilitate a proper decision on the merits." Friedlander v. Nims, 755 F.2d 810, 813, n.3 (11th Cir. 1985) (quoting, Conley v. Gibson, 355 U.S. 41, 48 (1957)).

In contrast, the Second Circuit has adopted an extremely restrictive and

inflexible approach to pleading securities fraud under 9(b). In Denny v. Barber, supra, the court required that plaintiff's complaint state specific paragraphs in documents that were alleged to be false, exact transactions, and describe such items as loans, including exact amounts of the loans that plaintiff considered "risky." 576 F.2d at 469. The Second Circuit recognized that other courts sustained complaints no more specific than the complaint in Denny. However, the court stated that it would follow its own decisions. 576 F.2d at 469.*

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* Plaintiff submits that, even if Denny v. Barber establishes the pleading standards under 9(b), the facts as pleaded in this case are clearly adequate under any standards. Goldman v. Belden, 754 F.2d 1059, 1069 (2d Cir. 1985). Thus, the "fraud by hindsight" label does not fit the instant facts.

This Court has repeatedly emphasized that "private securities actions provide 'a most effective weapon in the enforcement' of the securities laws and are 'a necessary supplement to Commission action.'" Bateman, Eichler, Hill, Richards, Inc. v. Berner, 53 U.S.L.W. 4737, 4740 (U.S. June 11, 1985) (No. 84-679) (quoting, J.I. Case, Co. v. Borak, 377 U.S. 426, 432 (1964)). The incongruous result engendered by the different standards for applying 9(b) hinders and ultimately defeats this policy. It encourages forum shopping and inequitable administration of the law, Sovern, supra, at 164; it delays litigation while parties argue about the sufficiency of the complaint; and it results in colorable cases being dismissed because pleaders cannot measure up to the standards created by an excessively rigid interpretation of the Rule. Id. at 150.

In the instant case, it is our contention that the rigid requirements of the Second Circuit concerning Rule 9(b) resulted in the unfair dismissal of a meritorious claim.

2. The complexity of contemporary fraud transactions requires a flexible application of rule 9(b), which is not followed by the Second Circuit, and which should be followed to ensure that meritorious claims are heard.

A strict application of Rule 9(b) does not further its underlying policies or the underlying policies of the Federal Rules.* Instead, it invites complicated pleading requirements, increased litigation and motion practice and hasty dismissals. Rule 9(b), created in 1937, was developed in order to reflect the common law rules of fraud pleading. Historically, fraud was a disfavored cause of action and common law rules required great particularity. Roberts, Fact Pleading, Notice Pleading and

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* Rule 1 of the Federal Rules requires that: "They shall be construed to secure the just, speedy, and inexpensive determination of every action." (A-209-210).

Standing, 65 Cornell L. Rev. 390, 395 (1980); Clark, Cases on Modern Pleading, 59 (1952). Fraud claims at common law grew out of disputes concerning fairness of face to face business transactions such as when a seller of goods misrepresented facts material to the value of such goods. In most contemporary securities fraud cases, however, plaintiffs have only indirect contact with defendants through impersonal market channels. Such conditions make it difficult for a plaintiff to plead with great particularity the details of an alleged fraud transaction. Harvard Note, supra, at 1436.

Rule 9(b) rests on three policies: desire to protect the reputations of innocent defendants; minimize strike suits; and provide notice to adverse parties. Sovern, supra, at 164. A review of these policies through the

application of Rule 9(b) reveals that a strict application does not necessarily encourage these goals.

Rule 9(b) is said to increase protection of reputations by deterring plaintiffs from filing complaints. Sovern, supra, at 171. A strict application of Rule 9(b), however, does not prevent unscrupulous plaintiffs from filing in the hope that the defendant will not challenge the complaint for insufficiency. Harvard Note, supra, at 1440. A strict application may have a chilling effect upon honest plaintiffs, who will be deterred from filing meritorious complaints for fear of not meeting 9(b) requirements. A more flexible application, however, will permit the case to at least reach the discovery stage so that an adequate determination of whether a claim is meritorious can occur.

Prospective harm to reputation depends on the assumption that vindication of the defendant in the public's eye will occur if the allegations are dismissed at the pleading stage. The public may look at such an early dismissal, however, as vindication through mere technicality. Sovern, supra at 172. Moreover, the reputation of a defendant may be so harmed by prior litigation that new litigation will not have a serious effect. In the instant case, defendants cannot suggest that a dismissal of the complaint protects their reputation. Some 51 lawsuits were filed in the federal courts against Merrill Lynch, Pierce, Fenner & Smith and other brokerage firms for improper conduct in the sale of Baldwin SPDA's. In addition, Shapiro v. Merrill Lynch & Co., Inc. and Merrill Lynch, Pierce, Fenner & Smith, Inc., C-1-85-0625 (S.D.

Ohio, W.D. filed March 1, 1985) was filed on behalf of Baldwin shareholders against Merrill Lynch.

The special requirements for pleading fraud under 9(b) create a situation of inequitable treatment of defendants under the law. Allegations of intentional torts such as assault, battery, false imprisonment, even allegations of gross negligence, impair a defendant's reputation. These allegations, however, are not pleaded with particularity. Sovern, supra, at 173. If the Federal Rules are designed to protect reputation, they should do so with consistency.

It is questionable whether Rule 9(b) should even elevate protection of reputation to such importance because of the substantive rights clause of the Rules Enabling Act (A-215-16). The Act serves as a reminder to minimize the substantive impact of the federal rules.

This argument is supported both by the Act itself, and its legislative history. 19 Wright, Miller and Cooper, Federal Practice and Procedure § 4509 at 139-140, n. 11 (1982). Justification for Rule 9(b) should more properly rest on rationales such as avoidance of strike suits and adequate notice. Even these goals, however, demonstrate that an unyielding application of Rule 9(b) is not necessary.

Deterrence of strike suits is a laudable goal. However, a stringent application of 9(b) creates greater difficulties than it cures. Some courts characterize Rule 9(b) as a rule requiring that facts be specific enough to insure that the plaintiff has adequately investigated the alleged fraud. The premise behind these opinions is that a complaint should seek to redress a

wrong, not find one. McGinty v. Beranger Volkswagon, Inc., 633 F.2d 226, 229 n.2 (1st Cir. 1980); Segal v. Gordon, 467 F.2d 602, 607-08 (2d Cir. 1972). The problem with this rationale is that these courts fail to consider the practical difficulties that plaintiffs encounter in acquiring factual details. Often, specific indications of securities fraud are hidden in internal memoranda, business projections and other records that are not easily obtainable. The Harvard Note aptly states:

> Few courts have explicitly considered . . . the practical difficulties in piercing the shroud of secrecy that surrounds most capital market transactions. Harvard Note, supra, at 1439.

Furthermore, the Federal Rules of Civil Procedure have other control mechanisms. Rules 16 (A-211-12) and 26(b) (A-212-13) enable judges to

limit the scope of discovery and Rule 56 allows for review of discovery material prior to dismissal (A-213-15). Here, plaintiff was denied even limited discovery (A-4-5, 6-8, 20-23).

A strict application of Rule 9(b) conflicts with the requirements of Rule 8 (A-210). The basic principle behind Rule 8 and the Federal Rules of Civil Procedure is to simplify the pleading process. Id. at 149. The plaintiff must only plead enough information so that the defendants can adequately respond to the allegations. The plaintiff need not plead evidence. Defendants can generally admit or deny allegations without the plaintiff supplying a list of details. Harvard Note, supra, at 1444. If the defendant is not able to respond, he can make a 12(e) motion for a more definite statement (A-211).

Rigid requirements of detailed factual pleadings invite hasty dismissals of meritorious claims and an increase in litigation while the plaintiff tries to amend the complaint to satisfy the Court's perceived interpretation of Rule 9(b). Harvard Note, supra at 1442.

3. Plaintiff's complaint and exhibits, having raised issues of fact concerning defendants' failure to disclose its liability for Baldwin-related transactions, such facts being peculiarly within the knowledge of defendants and discovery having been denied, should not have been dismissed by summary judgment.

Plaintiff was not required to prove any of the allegations of his complaint to defeat a motion for summary judgment. The question before the Circuit Court was whether triable issues of fact had been raised. This Court has recently reaffirmed its holding in Conley v. Gibson, 355 U.S. 41, 45-46 (1957), that "a court may dismiss a complaint only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations." Hishon v. King & Spalding, 104 S. Ct. 2229, 2233 (1984).

At bar, no affidavit was made in support of defendants' motion by any person having knowledge of the facts. No facts at all were set forth by defendants. The Circuit Court granted summary judgment upon the complaint, and exhibits annexed thereto and the exhibits furnished in support of and in opposition to the motion. The granting of summary judgment had to be based upon the inferences the Court drew from the documents before it, which are indeed susceptible to different interpretations. Such inferences the Court may not draw. It was not the trier of fact. Reasonable minds may differ.

The court's error was further compounded by denial of discovery.

Plaintiff alleges that defendants knew of their vast exposure to Baldwin prior to their first and second quarter 1983 reports of record earnings and

continued strength, which were relied on by plaintiff when he purchased. It is respectfully submitted that no court, without the benefit of additional facts flushed out by discovery, could summarily rule that "no relief could be granted under any set of facts that could be proved consistent with [these] allegations." Hishon v. King & Spalding, supra, 104 S. Ct. at 2233; accord, Adickes v. S.H. Kress & Co., 398 U.S. 144, 157 (1970); 6 J. Moore and J. Wicker, Moore's Federal Practice, ¶56.23, 1387, 1389-90 (2d Ed. 1982).

In a private civil action brought to enforce defendants' liability under the securities laws, where the facts are peculiarly within the knowledge of the defendants, "plaintiff is entitled to a trial." Subin v. Goldsmith, 224 F.2d 753, 757 (2d Cir.), cert. denied, 350 U.S. 883 (1955).

Subin held that where evidence must come largely from the defendants, where contrary facts are peculiarly within the opponents' knowledge and where a complicated state of facts exists, summary judgment should be denied. 224 F.2d at 757-58.

In Schoenbaum v. Firstbrook, 405 F.2d 215, 218 (2d Cir. 1968) (en banc), cert. denied, 395 U.S. 906 (1969) the Second Circuit stated that "issues as to the knowledge, intent, and motive" of defendants require a full trial. In describing the instant case as "fraud by hindsight", it appears that the Circuit Court found as a fact that defendants could not have had scienter in spite of the factual evidence submitted. The allegations concerning the individual defendants' intimate knowledge and the sources of plaintiff's information were repeatedly set forth in the complaint.

Defendants are the only ones who knew their motive, intent and scienter concerning the impact that their sales of Baldwin SPDAs would have upon Merrill Lynch's financials. It defies belief that other brokerage houses, with far less knowledge of Baldwin and its subsidiaries, ceased selling Baldwin SPDAs while Merrill Lynch rolled along, racking up its "record" earnings.

Defendants claimed that the earnings reflected set records in the first quarter and again in the second quarter. Merrill Lynch announced a 2-1 stock split, its dividend was raised and defendant Birk stated that Merrill Lynch would "live and thrive whatever the rules" (A-58). In short, defendants reported record earnings and profits, and prophesied a continuation thereof. At the same time they omitted to disclose that Merrill Lynch faced large

losses as a result of the wrongful acts and practices it engaged in concerning the sales of Baldwin SPDAs. They omitted to disclose that the collection of Baldwin's $90 million indebtedness to them was highly doubtful. As a result, Merrill Lynch's financials were overstated and misleading.

Did defendants' failure to make public its exposure to Baldwin SPDA purchasers meet the fraud requirements sufficient to impose liability under § 10(b) at the time of the above-referenced reports? If so, then the court's "fraud by hindsight" finding has been refuted. To resolve this question, one must determine defendants' motive, intent and knowledge concerning its disclosure, or lack of disclosure, about its Baldwin relationship.

In an attempt to ascertain the motive, intent and knowledge of defend-

ants and to "prove" defendants' scienter, from sources other than those publicly available, plaintiff noticed discovery. The limited discovery sought was particularly stated to be "in support of plaintiff's opposition to defendants' motion for summary judgment" and to "use the same on defendants' motion for summary judgment, now pending."

The District Court thereafter granted defendants' summary judgment and denied discovery (A-6-8). The Circuit Court affirmance agreed with the denial of discovery (A-20-23).

We believe that the granting of the motion for summary judgment was error for the reasons hereinabove set forth, including the denial of plaintiff's motion to take judicial notice of the exhibits setting forth further facts as

to defendants' awareness of its fraudulent conduct prior to plaintiff's purchases. When the granting of the motion for summary judgment was accompanied by a denial of discovery, the error was compounded.

The Second Circuit has repeatedly held that in complex securities litigations summary judgment should rarely be granted. Schoenbaum v. Firstbrook, supra, 405 F.2d at 218; Subin v. Goldsmith, supra; Colby v. Klune, 178 F.2d 872 (2d Cir. 1949); Fogelson v. American Woolen Co., 170 F.2d 660 (2d Cir. 1948); see also, Poller v. Columbia Broadcasting System, Inc., 368 U.S. 464 (1962) (antitrust). It has likewise been repeatedly held that this general maxim is even more stringently applied when no discovery has been had. Schoenbaum v. Firstbrook, supra; Subin v.

Goldsmith, supra. Gary Plastics Packaging Corp. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 756 F.2d 230, 236 (2d Cir. 1985) ("The harshness of the [summary judgment] remedy is exacerbated when the trial court refuses to allow plaintiff to conduct discovery").

In Schoenbaum, it was stated:

> The district court's grant of summary judgment against the plaintiff was accompanied by a refusal of his request for discovery. This court has indicated that summary judgment should rarely be granted against a plaintiff in a stockholder's derivative action especially when the plaintiff has not had an opportunity to resort to discovery procedures. The plaintiff typically has in his possession only the facts which he alleges in his complaint. Having little or no familiarity with the internal affairs of the corporation, he is faced with affidavits setting forth in great detail management's version of what actions were taken and what motives led the affiants to take these actions. Since the facts in such a case are exclusively

> in the possession of the defendants, summary judgment should not ordinarily be granted where the facts alleged by the plaintiff provide a ground for recovery, at least not without allowing discovery in order to provide plaintiff the possibility of counteracting the effect of defendants' affidavits. Indeed, in many stockholders' derivative actions there will be issues as to the knowledge, intent and motive which will require a full trial with an opportunity to observe the demeanor of the witnesses, and to conduct cross-examination in open court. In such cases summary judgment cannot be granted even after discovery has been had.

405 F.2d at 218 (citations omitted) (emphasis added).

Schoenbaum has since been cited with approval by the Second Circuit in an action brought under § 10(b). Wechsler v. Steinberg, 733 F.2d 1054, 1059 (2d Cir. 1984).

The observation made by Judge Learned Hand in Bozant v. Bank of New York, 156 F.2d 787 (2d Cir. 1946)

is particularly apropos:

> In conclusion we cannot avoid observing that the case is another mistaken effort to save time by an attempt to dispose of a complicated state of facts on motion for summary judgment. This is especially true when the plaintiff must rely for his case on what he can draw out of the defendant. It appears to be somewhat difficult to persuade the district courts of this; but we are satisfied that it is true. (Citation omitted).

Id. at 790.

CONCLUSION

It is respectfully submitted that the facts pleaded and referred to in the complaint, are sufficient to satisfy Rule 9(b). At the same time, these facts, if true, as plaintiff should have the opportunity to prove, raise material issues of fact as to Merrill Lynch's fraudulent conduct by its failure to

disclose its exposure as a result of its intimate and detailed involvement in the affairs of Baldwin, prior to plaintiff's purchases. Based on the facts alleged, and materials submitted below, the granting of summary judgment constituted reversible error.

For the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari should be granted.

Respectfully submitted,

STULL, STULL & BRODY
Attorneys for Plaintiff
6 East 45th Street
New York, New York 10017
(212) 687-7230

No. 85-36 (2)

Supreme Court, U.S.
FILED
JUL 5 1985
ALEXANDER L. STEVAS
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

MICHAEL CEASAR,

Petitioner,

-against-

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT
APPENDIX VOLUME

STULL, STULL & BRODY
Attorneys for Petitioner
6 East 45th Street
New York, New York 10017
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221pp

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UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

MICHAEL CEASAR,

Plaintiff,

- against -

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Defendants.

----------x

MEMORANDUM AND ORDER

CV 84-0435

(Wexler, J.)

APPEARANCES:

STULL, STULL & BRODY
Attorneys for Plaintiff
6 East 45th Street
New York, NY 10017

ROGERS & WELLS
Attorneys for Defendants
200 Park Avenue
New York, NY 10166

WEXLER, District Judge

This is an action for securities fraud. Defendants have made a motion "pursuant to Rules 9(b) and 12(b) of the Federal Rules of Civil Procedure,

for an Order dismissing plaintiff's complaint for failure to plead fraud with particularity, and for such other and further relief as this Court may deem just and proper." The motion is apparently based in part upon Rule 12(b)(6), dealing with the defense of failure to state a claim upon which relief can be granted. Since the parties have presented matters outside the pleadings, we will, pursuant to Rule 12(b), treat this as a motion for summary judgment under Rule 56, and give all parties reasonable opportunity to present all material made pertinent to such a motion by Rule 56.

It is, therefore,

ORDERED, that defendants may file any additional papers they wish to file under Rule 56(b), within twenty (20) days of notice of this order; and it is further

ORDERED, that plaintiff may file any additional papers he wishes to file under Rule 56(c), within fifteen (15) days of service upon plaintiff of defendants' papers, or within fifteen (15) days of receiving notice that defendants do not intend to file such papers.

SO ORDERED.

LEONARD D. WEXLER
UNITED STATES DISTRICT JUDGE

Dated: Uniondale, New York
July 27, 1984

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

MICHAEL CEASAR,

Plaintiff,

- against -

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Defendants.

----------x

ORDER

CV 84-0435

(Wexler, J.)

APPEARANCES:

STULL, STULL & BRODY
Attorneys for Plaintiff
6 East 45th Street
New York, NY 10017

ROGERS & WELLS
Attorneys for Defendants
200 Park Avenue
New York, NY 10166

WEXLER, District Judge

All discovery is stayed pending disposition of the pending motion for summary judgment. The Court reserves the right to permit discovery in the

future if, after plaintiff has submitted papers opposing the motion, such discovery should appear appropriate.

SO ORDERED.

LEONARD D. WEXLER
UNITED STATES DISTRICT
JUDGE

Dated: Uniondale, New York
September 20, 1984

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

MICHAEL CEASAR,

Plaintiff,

against

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Defendants.

----------x

MEMORANDUM AND ORDER

CV 84-0435

(Wexler, J.)

APPEARANCES:

STULL, STULL & BRODY
Attorneys for Plaintiff
6 East 45th Street
New York, NY 10017

ROGERS & WELLS
Attorneys for Defendants
200 Park Avenue
New York, NY 10166

WEXLER, District Judge

This is an action for securities fraud. Defendants moved to dismiss for failure to allege fraud with particularity. We have converted this

motion into one for summary judgment.

Upon examining all papers submitted, we find that the motion for summary judgment should be granted. This is essentially an action for "fraud by hindsight". The papers submitted do not suggest any reasonable basis for believing that statements made by the defendants were made with knowledge that such statements would be misleading. To permit plaintiff to engage in discovery would be to permit a "fishing expedition", at enormous expense to the defendants.

Defendants' motion for summary judgment is granted. This action is dismissed. The Clerk shall enter judgment accordingly.

SO ORDERED.

LEONARD D. WEXLER
UNITED STATES DISTRICT JUDGE

Dated: Uniondale, New York
October 10, 1984

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

MICHAEL CEASAR,

Plaintiff,

- against -

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER

Defendants.

----------x

FILED IN
CLERK'S OFFICE
U.S. DISTRICT
COURT E.D.N.Y.
LONG ISLAND
OFFICE
OCT 18, 1984

CV-84-0435
LDW

JUDGMENT

A Memorandum and Order of Hon. Leonard D. Wexler, United States District Judge, having been filed on October 15, 1984, granting defendants' motion for summary judgment, and directing the Clerk to enter judgment dismissing the complaint, it is

ORDERED and ADJUDGED that the plaintiff take nothing of the defendants; that the defendants' motion for summary judgment is granted; and that the

complaint is dismissed.

DATED: Uniondale, N.Y.
October 18, 1984

ROBERT C. HEINEMANN
Clerk of Court

By: _____
JOSEPH DiTALIA
Deputy-in-Charge

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

MICHAEL CEASAR,

Plaintiff,

against

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Defendants.

----------x

MEMORANDUM AND ORDER

CV 84-0435

(Wexler, J.)

APPEARANCES:

STULL, STULL & BRODY
Attorneys for Plaintiff
6 East 45th Street
New York, NY 10017

ROGERS & WELLS
Attorneys for Defendants
200 Park Avenue
New York, NY 10166

WEXLER, District Judge

This is an action for securities fraud. Defendants moved to dismiss for failure to allege fraud with particularity. We converted the motion into one

for summary judgment.

Plaintiff was a purchaser of defendant Merrill Lynch's stock. Plaintiff contends that the price of the stock was inflated as a result of failure by the defendants to disclose potential financial difficulties for Merrill Lynch arising from its dealings with Baldwin Insurance Subsidiaries.

In deciding this motion, we are aware that allegations of fraud generally cannot be based upon information and belief, and that although this rule is relaxed as to matters peculiarly within the adverse parties' knowledge, the allegations must then be accompanied by a statement of the facts upon which the belief is founded. Segal v. Gordon, 467 F.2d 602, 608 (2d Cir. 1972). We are also aware that material submitted in connection with a motion for summary judgment should be viewed in the light

most favorable to the party opposing the motion.

Upon examining all papers submitted, we find that the motion for summary judgment should be granted. This is essentially an action for "fraud by hindsight". The papers submitted do not suggest any reasonable basis for believing that defendants made material misstatements or omissions of fact concerning Merrill Lynch's financial prospects with knowledge or reckless disregard of the possibility that such would be misleading. To permit plaintiff to engage in discovery would be to permit a "fishing expedition" at enormous expense to the defendants.

For the above reasons, we granted defendants summary judgment on October 10, 1984.

Plaintiff's motion for reconsideration is denied.

SO ORDERED.

LEONARD D. WEXLER
UNITED STATES DISTRICT JUDGE

Dated: Uniondale, New York
November 9, 1984

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

MICHAEL CEASAR,

Plaintiff,

-against-

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Defendants.

----------x

ORDER

CV 84-0435

(Wexler, J.)

APPEARANCES:

STULL, STULL & BRODY
Attorneys for Plaintiff
6 East 45th Street
New York, NY 10017

ROGERS & WELLS
Attorneys for Defendants
200 Park Avenue
New York, NY 10166

WEXLER, District Judge

Plaintiff having moved for relief from judgment pursuant to Rule 60(b), and the Court lacking jurisdiction to rule upon such a motion, and the Court

having determined that the Court would be inclined to deny such motion if it had jurisdiction to rule upon it, it is hereby

ORDERED, that this Court declines to request the Court of Appeals to remand this case, and it is further

ORDERED, that plaintiff's motion for relief from judgment is deemed moot on the ground that this Court lacks jurisdiction to rule upon it.

SO ORDERED.

LEONARD D. WEXLER
UNITED STATES DISTRICT JUDGE

Dated: Uniondale, New York
March 8, 1985

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

----------x

MICHAEL CEASAR,

Plaintiff-Appellant,

v.

MERRILL LYNCH & CO., INC., et al.,

Defendants-Appellees.

----------x

84-9015

NOTICE OF MOTION

For Expansion of Record or To Have This Court Take Judicial Notice of Documents Filed In Related Proceedings

MOTION BY: STULL, STULL & BRODY
6 East 45th Street
New York, New York 10017
Of Counsel: ROBERT A. STULL
(212) 687-7230

OPPOSING COUNSEL: ROGERS & WELLS, ESQS.
260 Park Avenue
New York, New York 10166
Of Counsel: LOUISE SOMMERS, ESQ.
(212) 878-8000

Has consent of opposing counsel:

A. been sought? x Yes ___ No

B. been obtained? ___ Yes x No

Has service been effected? x Yes ___ No

Is oral argument desired? x Yes ___ No

(Substantive Motions Only)

Requested return date: April 4, 1985
or earlier

(See Second Circuit Rule 27(b))

Has argument date of appeal been set:

A. by scheduling order? ___Yes ___No

B. by firm date of argument notice? _x_ Yes ___No

C. If Yes, enter date: April 4, 1985.

Judge or agency whose order is being appealed:

HON. LEONARD D. WEXLER, UNITED STATES DISTRICT JUDGE, EASTERN DISTRICT OF NEW YORK

Brief statement of the relief requested:

Appellant seeks to expand record to including in Joint Appendix four (4) documents (3) filed in two (2) District Courts subsequent to the filing of the of the Notice of Appeal herein or alternatively to have this Court take judicia notice of the facts contained in such documents.

By: (Signature of Attorney)

ROBERT A. STULL

Appearing for: (Name of Party)

MICHAEL CEASAR -- Plaintiff

-- ORDER --

IT IS HEREBY ORDERED that the motion be and it hereby is ~~granted~~ denied.

IRVING R. KAUFMAN

Seal: United States Court of Appeals
Filed March 25, 1985
Elaine B. Goldsmith, Clerk
Second Circuit

3/25/85

UNITED STATES COURT OF APPEALS
Second Circuit

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 8th day of April one thousand nine hundred and eighty-five.

Present:

HONORABLE IRVING R. KAUFMAN,

HONORABLE WILLIAM H. TIMBERS

HONORABLE JON O. NEWMAN,

Circuit Judges.

----------x

MICHAEL CEASAR,

Plaintiff-Appellant, 84-9015

-against-

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Defendants-Appellees.

----------x

Appeal from the United States District Court for the Eastern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Eastern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged and decreed that the judgment of said District Court be and it hereby is affirmed.

1. Ceasar asserts that his complaint, along with evidence presented to the district court, raised material issues of fact, and thus that summary judgment was improperly granted. We disagree. A careful review of the documentary evidence adduced below impels us to the agree with

the district court's characterization of the complaint as one "alleging fraud by hindsight," Denny v. Barber, 576 F.2d 465, 470 (1978). Even assuming all factual questions were resolved in Ceasar's favor, we do not believe his claim was viable.

2. Neither do we believe that it was error for the district court to deny Ceasar's request for discovery. Assessing a similar claim in Denny v. Barber, supra, Judge Friendly wrote that "there . . . must be more than vague allegations that, as shown by subsequent developements, the corporation's true financial picture was not so bright in some respects as its [earlier statements] had painted." Id. at 470. Because Ceasar's conclusory allegations did not exceed this minimum standard,

his discovery request was properly denied.

3. Accordingly, the judgement of the district court is affirmed.

IRVING R. KAUFMAN

WILLIAM H. TIMBERS,

JON O. NEWMAN,

Circuit Judges.

N.B.: Since this statement does not constitute a formal opinion of this court and is not uniformly available to all parties, it shall not be reported, cited or otherwise used in unrelated cases before this or any other court.

Stamp/Seal: "United States Court of Appeals
Filed April 8, 1985
Elaine B. Goldsmith
Second Circuit"

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK
----------x

MICHAEL CEASAR,

Plaintiff,

v.

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Defendants.

----------x

84 Civ. 0436 (LDW)

CLASS ACTION

AMENDED COMPLAINT

TRIAL BY JURY DEMANDED

Plaintiff, for his amended complaint, alleges upon information and belief, except as to paragraph 3, which is alleged on knowledge:

1. The jurisdiction of this Court is founded upon Section 27 of the Securities Exchange Act of 1934 (15 USC 78aa) (the "Act"). This action is brought to enforce defendants' liability for misconduct created by Section 10b of the Act (15 USC 78j (b)) and Rule 10b-5 of the

Securities and Exchange Commission (17 CFR 240.10b-5). The acts and practices complained of occurred in whole or part in the Eastern District of New York.

2. Class Action Allegations

(1) The action is properly maintainable as a class action within Rule 23 (a) and (b) subdivision (1) (B), and (3) of the Federal Rules of Civil Procedure.

(2) (i) and (ii) The number of members of the class is not known. It is believed that they exceed several thousand and are located throughout the United States and in several foreign countries. The members of the class are so numerous as to make it impractical to bring them all before the Court. The class is comprised of the purchasers of

the shares of Merrill Lynch & Co. Inc. ("Merrill Lynch") who purchased such shares on the public market on or about and between April 26, 1983 and September 26, 1983 (the "class period") at prices artificially inflated by the defendants as a result of false or misleading statements in or material omissions from Merrill Lynch's reports required by law, which, among other reports, were disseminated by Merrill Lynch to its shareholders and the financial community in that period.

(iii) The basis upon which it is claimed that plaintiff will fairly and adequately protect the interests of the class is that plaintiff's claims are typical of the class, in that plaintiff and the other members of the class were induced to purchase their securities in the period complained of, in an artificially inflated market

and/or market climate created by the defendants by means of the wrongful acts herein complained of; that he is not associated in any way, shape or form with the defendants; that his attorneys are experienced in this type of litigation and will prosecute the same diligently on behalf of the plaintiff and the class he represents; and that neither plaintiff nor his attorneys have any adverse interests to the claims of Merrill Lynch's stockholders comprising the class.

(iv) The questions of law and fact common to the class are:

(a) Whether defendants' statements to the public and to the financial community, on or about and between April 26, 1983 and September 26, 1983 contained false or misleading statements or material omissions with respect to the earnings, financial

condition, transactions and prospects of Merrill Lynch;

(b) Whether defendants artificially inflated the market price for Merrill Lynch's shares or created an artificial market climate therefor in said period;

(c) Whether plaintiff and other members of the class similarly situated were induced to purchase their shares in Merrill Lynch by the wrongful acts of the defendants complained of;

(d) Whether the wrongful acts of the defendants complained of constituted violations of the Act and the Rules and Regulations of the SEC applicable thereto; and

(e) Whether plaintiff and other shareholders of Merrill Lynch similarly situated were damaged by the wrongful acts of the defendants

complained of.

(v) An adjudication of plaintiff's claims would, as a practical matter, be dispositive of the interest of all shareholders of Merrill Lynch who purchased their shares in the period complained of and are not parties to the adjudication, in that all such purchasers bought their shares in said period based upon the same operative facts as did the plaintiff. No other litigation concerning the controversy has been commenced by or against members of the class, as far as plaintiff is informed. It is claimed that questions of law and fact common to the members of the class predominate over any questions affecting only individual members and that class relief is superior to other forms of relief. Plaintiff knows of no difficulties likely to be encountered in the management of the action as a class action.

CAUSE OF ACTION

3. Plaintiff is a resident of the County of Nassau, State of New York. Plaintiff purchased 100 shares of Merrill Lynch on July 5, 1983, 100 shares on July 28, 1983 and 150 shares on September 13, 1983 on the New York Stock Exchange during the class period. In making his purchase, plaintiff relied upon the integrity of the market and the market climate generated by defendants for Merrill Lynch shares.

4. Defendant Merrill Lynch is and at the times complained of was a Delaware corporation, primarily engaged in business as a securities broker, through its wholly owned subsidiary, Merrill Lynch, Pierce, Fenner & Smith, Inc. ("MLPFS"), with its principal executive offices at One Liberty Plaza, 165

Broadway, New York, NY 10080.

5. (a) The individual defendants held the following positions with Merrill Lynch at the times complained of:

ROGER E. BIRK - Chairman of the Board of Directors and Chief Executive Officer;

DAKIN B. FERRIS - Executive Vice President and Director;

WILLIAM A. SCHREYER - President, Director and Chief Operating Officer.

(b) By virtue of their management positions and memberships on the Board of Directors of Merrill Lynch the said individual defendants were at all relevant times controlling persons of Merrill Lynch and its subsidiaries within the meaning of Section 15 of the Securities Act of 1933, 15 USC 77o and Section 20 of the 1934 Act, 15 USC 78t.

(c) The said individual defendants knew of and authorized the illegal conduct set forth herein.

6. Defendants knowingly and with intent to defraud plaintiff and other stockholders of Merrill Lynch similarly situated, caused the wrongful acts and material omissions herein complained of in manner hereinafter alleged or are chargeable therewith.

7. By the acts and practices complained of and the use of the means and instrumentalities of interstate commerce, or the mails, defendants employed devices, schemes and artifices to defraud, made untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, and defendants engaged in transactions, practices or a course of business which would and did operate as a fraud and deceit upon the

plaintiff and other shareholders of Merrill Lynch similarly situated who purchased their Merrill Lynch shares in the period complained of.

8. At all relevant times, Baldwin-United Corp. ("Baldwin") was and is a diversified financial services business whose activities include insurance. The following companies were wholly owned subsidiaries of Baldwin: University Life Insurance Company of America ("University Life"), S & H Life Insurance Company ("S&H"), National Equity Life Insurance Company ("National Equity"), all of which were organized under the laws of the State of Indiana, and National Investors Life Insurance Company ("NILIC"), National Investors Pension Insurance Company ("NIPIC") and Mount Hood Pension Insurance Company ("Mount Hood"), all of which were organized under the laws of

the State of Arkansas. Each company dealt in insurance and was subject to the regulatory authorities of the insurance department of the state of its organization. Such Baldwin subsidiaries are referred to collectively herein as Baldwin Insurance Subsidiaries.

9. The Baldwin Insurance Subsidiaries began selling single premium deferred annuities ("SPDA") in 1979. Merrill Lynch, MLPFS and the individual defendants decided that it would be a source of great profit for them to use their network of offices and account representatives to enter the business of selling SPDAs, and they did. They used as their vehicles various wholly owned subsidiaries of Merrill Lynch in various states (hereinafter sometimes collectively referred to as "Merrill Lynch").

10. Merrill Lynch, through MLPFS and other wholly owned subsidiaries engaged in the sale of SPDAs emanating from Baldwin and its subsidiaries. These sales were made prior to and during the class period. By April 15, 1983 SPDA sales through Merrill Lynch and its subsidiaries had reached $1.5 billion.

11. In many instances account executives employed by MLPFS or Merrill Lynch were instructed by Merrill Lynch or MLPFS in standard techniques of soliciting their brokerage customers in order to promote and sell SPDAs to them, from which sales either Merrill Lynch or its subsidiaries received commissions and other compensation, profits or emoluments. Merrill Lynch's employees, agents and subsidiaries, at the direction of and with the help of Merrill Lynch or

MLPFS, prepared or distributed advertising, promotional and solicitation material advertising the said SPDAs as safe, risk-free and guaranteed investments. The SPDAs contracted to pay an initial fixed rate of interest substantially higher than market rates for the first year, and substantially lower rates for subsequent years and were to accumulate income tax free until the investor began to receive payments, usually at retirement. The SPDAs stated that holders were to have the right to receive higher rates of interest, which the Baldwin Insurance Subsidiaries stated they intended to pay but as a matter of discretion.

12. The Baldwin Insurance Subsidiaries' SPDAs sold by Merrill Lynch, MLPFS, their employees, agents and subsidiaries, were not registered under the Securities Act of 1933, Section 5 of

which prohibits the sale of any security unless such security is registered or unless an exemption from the registration requirement is available. Under the Securities Act purchasers of unregistered securities would have the absolute right to rescission and to obtain a full refund of the purchase price. Merrill Lynch would have to bear the resultant losses.

13. The Baldwin Insurance Subsidiaries' SPDAs sold by Merrill Lynch, its agents and subsidiaries, did not qualify for any of the exemptions available under any provision of the 1933 Act, including Sections 3 and 4 thereof, for the following reasons, among others:

(a) The SPDAs were marketed primarily as investment vehicles, and in a manner typical of that involving the offer and sale of securities.

(b) The SPDAs were promoted by advertisements and literature which emphasized high first year contractual interest and the possibility of interest higher than contractual rates in later years at the discretion of the issuer.

(c) The SPDAs were sold primarily to brokerage house customers by brokerage houses, whose representatives touted the SPDAs as investments rather than as annuities, emphasized the tax deferred accumulation of high contractual and discretionary interest and the ability to withdraw funds, and utilized techniques or descriptions typical of securities sales as opposed to traditional annuity sales.

(d) The SPDAs permit a purchaser to withdraw his money at no penalty if the discretionary interest rates do not achieve certain minimum levels, further evidencing the import-

ance of interest rates as the primary selling feature of the SPDA.

(e) The Baldwin Insurance Subsidiaries assumed no material mortality risk under the SPDAs because the guaranteed annuity conversion rates are so low that the guarantee is, in economic reality, a sham.

(f) Purchasers of SPDAs may take advantage of investment choices usually associated with the acquisition of securities, e.g., they would have the right to change their investment vehicle by redeeming their SPDAs whenever market interest rates or returns from other securities were higher and could thus redeploy their capital, as they deemed most advantageous.

(g) The terms of the SPDAs and the promotion thereof implied that the Baldwin Insurance Subsidiaries would continue to pay interest at annual rates

in excess of market rates of alternative investments in securities because of the provision that SPDAs were redeemable without any payment penalty only when the interest rates paid were below the contractual rate.

(h) The ability of purchasers to earn anticipated rates of interest and receive their capital on the SPDAs herein referred to depended on the investment portfolios of the respective Baldwin Insurance Subsidiaries and the investment acumen of those persons controlling such investments and were subject to the financial performance and the needs of Baldwin.

(i) Instead of acting as an intermediary between the Baldwin Insurance Subsidiaries and the individual purchaser of annuities, Merrill Lynch and its subsidiaries, in order to maximize their commissions or compensation

from the SPDAs, became the holder of a group annuity policy or policies and issued to each purchaser a certificate originating with a Merrill Lynch subsidiary, creating the impression that Merrill Lynch itself or acting jointly with the particular Baldwin Insurance subsidiary, was the issuer of the annuity.

(j) Although the Baldwin Insurance Subsidiaries held themselves out to be life insurance companies, they were not so, in fact, since they sold little, if any, life insurance.

14. In September, 1981, Merrill Lynch contracted to sell AMIC Corporation ("AMIC"), a North Carolina corporation engaged in the finance business, to Baldwin, with closing to take place in December, 1981. In connection with such contract, Merrill Lynch received a

plethora of audited and unaudited financial statements and information, a substantial portion of which was not publicly available and by which Merrill Lynch became intimately familiar with the financial condition of Baldwin and its subsidiaries. In addition, at the December 1981 closing, Merrill Lynch received a put agreement under which Baldwin undertook to meet certain financial obligations with respect to purchasing preferred shares and warrants received by Merrill Lynch as part of its consideration for the sale of AMIC, which provided, inter alia, that if such obligations were not met, Merrill Lynch was to receive a promissory note of not less than $31,000,000 in principal amount. Thus, Merrill Lynch, to protect its interest as a creditor, was required to and did monitor and become aware of the deteriorating financial condition

and continuing capital erosion and losses of Baldwin and of the Baldwin Insurance Subsidiaries. Merrill Lynch became the owner and holder of approximately $90,000,000 face value notes of Baldwin and/or its subsidiaries. As a result, Merrill Lynch, as a substantial and continuing creditor, became generally aware of and recklessly disregarded Baldwin's financial difficulties, and the inability of Baldwin and the Baldwin Insurance Subsidiaries to meet either the requirements of regulatory authorities or obligations of Baldwin and its subsidiaries on the aforesaid notes and under the SPDAs.

15. Prior to and during the class period, Merrill Lynch, its officers, directors, subsidiaries and affiliates had knowledge of the following aspects and the following material adverse

information with regard to Baldwin and the Baldwin Insurance Subsidiaries and the SPDAs:

(a) In order to consummate Baldwin's purchase in 1981 of MGIC Investment Corp. ("MGIC") for $1.2 billion, Baldwin arranged short-term bank loans of over $1/2 billion. Due to its financial difficulties, Baldwin repeatedly postponed the stated target dates for repayment thereof, and prior to and during the class period failed to repay such bank loans although it had reported that the MGIC acquisition cost would be generated internally and that all bank loans would be paid off in 1982. During the process of Baldwin's acquisition of MGIC, Merrill Lynch, its subsidiaries or affiliates, participated in and aided in such acquisition. In the course of their involvement in such purchase they

monitored, and had full knowledge of, Baldwin's financial condition.

(b) Between December, 1981 and March, 1982 when it ultimately acquired MGIC, Baldwin milked its insurance subsidiaries of nearly $1/2 billion in cash, and for such cash assigned to Baldwin Insurance Subsidiaries obligations or equities of Baldwin or other Baldwin subsidiaries which were of questionable value.

(c) Between 1979 and 1983, the Baldwin Insurance Subsidiaries collectively owned approximately $900,000,000 in securities of other Baldwin affiliates or subsidiaries. The value of such securities declined to the extent that successively in December 1981 and June 1982, the Arkansas Insurance Department found that the required surpluses of certain of the Baldwin Insurance Subsidiaries had been eroded

and compelled Baldwin to replace said erosions by escrowing $70 million to ensure contribution of additional assets to their capital. Such replacements, to the extent made, consisted of securities of other Baldwin subsidiaries subject to the same financial problems and deficiencies. Merrill Lynch knew and recklessly disregarded that all the Baldwin Insurance Subsidiaries faced the same problem for the same reasons.

(d) During the 1979-1983 period, the Baldwin Insurance Subsidiaries had been paying an average interest rate on their SPDAs substantially higher than the income said subsidiaries were earning on the monies received from purchasers, after deducting commissions and other expenses and costs of overhead allocable to the administration of the SPDAs. For example, the Baldwin Insurance Subsidiaries had been paying an

average of 13.6% on the amount deposited for the SPDAs while earning only an estimated 9% to 10% on the money left after paying commissions. Thus each new sale of a SPDA created a loss and a charge to surplus. Said Baldwin Insurance Subsidiaries had been losing money at the rate of $135,000,000 per year on the 163,000 SPDAs that they had sold in that period through Merrill Lynch and others in the face amount of $3.6 billior. In order to conceal these continuing losses, Baldwin sold securities in its portfolio at distress prices using the proceeds to add to the capital base of the Baldwin Insurance Subsidiaries. Further losses accumulated and the resulting financial stringencies of Baldwin halted these infusions of capital. Thus, said subsidiaries could not exercise their contractual right to lower the interest payments without

causing SPDA owners to call for repayment of their principal, a cash drain which the Baldwin Insurance Subsidiaries could not meet.

(e) Baldwin had made the disastrous negative profit situation referred to in subparagraph (d) above appear to be profitable by questionable accounting and tax procedures, such as improperly calculating deferred policy acquisition costs, $405,000,000 of which had to be written off in the first quarter of 1983, crediting earnings to a subsidiary taxed at a low rate and charging expenses from selling the annuities to a subsidiary with a high tax rate, improperly increasing reserves related to said subsidiary's single premium deferred annuity business, and, in the process, utilizing some of the Baldwin Insurance Subsidiaries to reinsure risks assumed by such subsidiaries. In

fact, Baldwin's method of accounting for SPDAs had been criticized by its auditors in 1982. In 1983, because of the above, substantial write-offs were required which had a negative cash impact of at least $75,000,000. In addition, in the second quarter of 1983, a further loss of $31,900,000 from the SPDA business was anticipated to be incurred because of the negative investment spread.

(f) Baldwin's wholly owned insurance brokerage firm, Bayly, Martin and Fay, was carried on Baldwin's books during the 1979-1983 period at $44,000,000 more than its value. Moreover, $60,000,000 face value of Bayly, Martin debentures had a real value of substantially less than that, were not freely marketable and had been sold by Baldwin to one of the Baldwin Insurance Subsidiaries to obtain cash for the parent company.

(g) Knowing that purchasers of SPDAs relied on the financial strength and profitability of Baldwin and believed that the Baldwin Insurance Subsidiaries were part of a financially secure and profitable enterprise, Merrill Lynch failed to disclose the adverse impact on Merrill Lynch of the fact that Baldwin's financial condition was precarious, that it was not able to pay its debt, that it was not able to meet the payment requirements to Merrill Lynch under the AMIC sale, and that prior to September 1982 the State of Texas had refused to allow Baldwin to file a registration of the sale of its securities because the State of Texas questioned the ability of Baldwin to pay its debt.

(h) That the SPDAs and Merrill Lynch's marketing thereof emphasized the possibility of earning higher rates of interest in subsequent

years without disclosing that the actual rate of interest was discretionary and tied to market forces.

16. Merrill Lynch knew of and recklessly disregarded various special reports available to it which, inter alia, specifically described the illiquidity and problems of the Baldwin Insurance Subsidiaries. Said reports were generally available to analysts employed by Merrill Lynch but not to plaintiff and the class members.

17. Merrill Lynch violated certain state statutes and regulatory requirements by offering SPDAs without being licensed and by unlawfully referring to, and describing inaccurately state insurance guaranty benefits. Thus, Merrill Lynch also violated Federal law by its sale of SPDAs which were in truth and

fact unregistered securities.

18. Insurance regulatory authorities in several states began investigations into the financial practices of the Baldwin Insurance Subsidiaries resulting in remedial orders and limitations being placed on said subsidiaries, which information was available to and known by Merrill Lynch.

19. In January, 1983, two major brokerage firms advised their account representatives to stop or curtail the promotion and/or sale of Baldwin Insurance Subsidiaries SPDAs. Defendants, however, continued their promotion and sale of said SPDAs, although they well knew the facts and circumstances herein alleged.

20. To promote, solicit sales and sell the SPDAs in the class period, Merrill Lynch directly and through its agents and subsidiaries instructed its account representatives to use certain promotional material, sales instruction kits, brochures and other printed material supplied by it to all its offices. Merrill Lynch prepared such kits or collaborated with the Baldwin Insurance Subsidiaries or others in the preparation of such items, or used items supplied by the said subsidiaries or others and adopted said items as its own sales tools. Merrill Lynch had knowledge of or recklessly disregarded that said sales tools contained false and misleading misrepresentations and material omissions. Said brochures, inter alia, intentionally misrepresented that the purchaser of a Baldwin Insurance Subsidiary SPDA emanating from one

of the subsidiaries, i.e., University Life, was backed by the financial resources of all the insurance companies combined, that all of such companies collectively guaranteed interest rates and payments and guaranteed the right of cancellation and withdrawal of all monies deposited plus accrued earnings, without company imposed charges. Said brochures emphatically guaranteed, but misrepresented the safety of the SPDA investments, and stated, among other things, as follows:

> "We currently have $1 billion in cash (C.D.'s, Treasury Bills) to meet any policyholder liquidity needs.
>
> Our SPDAs are virtually risk free.
>
> Their strength is in the quality and liquidity of our assets. Baldwin insurance companies selling SPDAs have investment portfolio with a market value of approximately $3.2 billion. Included in the long-term portfolio are top quality preferred stocks and bonds, 85% of which are "A" rated or

> better. Unlike many competitors, we do not depend on lower S&P ratings to achieve higher yields.
>
> If every SPDA holder were to request payment tomorrow, Baldwin's insurance companies have sufficient readily marketable investments to pay out 100 cents on the dollar in cash."

The facts were that (a) the purchaser was investing in an SPDA emanating from a single Baldwin Insurance Subsidiary; (b) his sole reliance for financial safety was on the net assets and reserves of such single subsidiary; (c) there was not $1 Billion in cash" to meet "any policyholder liquidity needs"; (d) the investment portfolio did not have a market value of approximately $3,200,000,000 nor was there $1,000,000,000 in bank CD's and Treasury Bills with maturities of less than one year which would insure liquidity; and finally (e) the Baldwin Insurance

Subsidiaries did not have "sufficient readily marketable investments to pay out 100 cents on the dollar in cash."

21. As part of its securities brokerage business, Merrill Lynch maintained a research and securities analysis staff which investigated, surveyed, monitored and made recommendations of various securities in various industries to Merrill Lynch customers.

22. By virtue of Merrill Lynch's position as a substantial and continuing creditor of Baldwin and by virtue of its research and analysis activities, defendants knew or should have known, or with notice thereof recklessly disregarded the facts cited in paragraphs 13 through 21, supra, and the financial difficulties of Baldwin and its insurance and other subsidiaries and their

inability to meet their obligations under the SPDAs sold by defendants.

23. Merrill Lynch continued its sales of the said SPDAs although it knew of the financial difficulties and problems of Baldwin and the Baldwin Insurance Subsidiaries and knew of the material adverse financial information concerning their liquidity problems above alleged. Ultimately the regulatory authorities of Arkansas put NILIC, NIPIC and Mount Hood under rehabilitation proceedings and the Indiana regulatory authorities placed University Life, S&H and National Equity in rehabilitation, because of the partial disclosures concerning the misleading statements and material omissions with reference to SPDAs heretofore alleged. The regulatory authorities also reduced the interest payments on the SPDAs and

suspended the right of SPDA owners to withdraw their principal, notwithstanding that the interest rates had been reduced below contractual minimums. As a result, payments of principal and interest were placed in jeopardy.

24. On or about April 26, 1983 Merrill Lynch announced that its first quarter profits had more than quadrupled; that the first quarter dividend would be increased and that there would be a two for one stock split. Defendant Birk stated that Merrill Lynch was "prepared to live and thrive whatever the rules [governing the financial business]".

25. Further supporting Merrill Lynch's bullish first quarter announcement and statement made by its Chairman of the Board, was the First Quarter

Report, dated May 12, 1983 (Exhibit "1", annexed), for the quarter ended April 1, 1983, which contained the growth figures announced on April 26, 1983, and further expanded them. Thus, the First Quarter Report, in addition to stating that Merrill Lynch's net earnings as compared to those of the same quarter a year earlier, rose 322.6% also stated that Earnings Per Share rose 303.9% (280.3% fully diluted). The First Quarter Report actually reported that the "gain in net earnings was held to 323% because of an increase in the effective tax rate to 47.0% from 34.6% in the comparable 1982 quarter." (Emphasis added).

26. The First Quarter Report disseminated to shareholders and the public on or about May 12, 1983 over the signatures of defendants Birk and Schreyer not only failed to note the

adverse financial problems of which Merrill Lynch is charged with being aware of vis-a-vis Baldwin, but went out of its way to point out that the record earnings posted were achieved based upon all of the facets of its business. Thus, the Report stated:

> "While the strong stock market and record trading volume helped us achieve these records, it is once again a case of broad-based strength generated by the many different services and products we offer our customers. It's also significant that our real estate activities, which operated at a loss in the year-ago quarter, are now in the black for the third quarter in a row." (Emphasis added).

27. Continuing the same course of fraudulent conduct, on July 26, 1983, Merrill Lynch publicly announced that its earnings in the second quarter more than tripled on a 38% rise in revenue. On July 27, it publicly announced net

income for the quarter at $112,225,000 and net income for the six months at $239,119,000 or $2.71 per share. These publicly reported announcements were made within one or two days, respectively, prior to plaintiff's second purchase (supra, p. 5).

28. Once again, Merrill Lynch not only failed to note its problems with Baldwin of which it was aware, but went out of its way to point out that its announced record earnings posted were achieved based upon its generally broad based earnings. Thus, the Second Quarter Report, dated August 11, 1983, for the period ending July 1, 1983 (Exhibit "2", annexed), over the signatures of defendants Birk and Schreyer stated:

> "Our results for the second quarter and first half were the best in our history."

and

> "These results stem from a generally very strong showing in the great majority of our activities."
> (Emphasis added)

Once again, Merrill Lynch pointed out that their gain for the quarter was "held" to only 211% as compared to the prior year's quarter because the effective tax rate had risen by nearly 20% from the prior year's quarter.

29. Said announcements and reports were materially misleading inasmuch as at the time of the announcements and reports defendants knew or should have known and omitted to disclose the problems with the Baldwin Insurance Subsidiaries SPDAs hereinabove described; that all persons who purchased Baldwin Insurance Subsidiaries' SPDAs would sustain substantial damages; would lose the contractual interest rates promised;

that Merrill Lynch and/or MLPFS would be held accountable for substantial losses; that Merrill Lynch's status as a creditor of Baldwin was questionable in that there was no likelihood that Merrill Lynch could recover the sums owed to it, and the earnings, profits and operations of Merrill Lynch would be adversely affected.

30. For the reasons hereinabove set forth, during the class period, defendants knew or should have known and omitted to disclose the problems with Baldwin and the Baldwin Insurance Subsidiaries hereinabove described and the adverse effect thereof on Merrill Lynch as set forth in the preceding paragraph.

31. Having publicly emphasized its growth in the first quarter and first

half of 1983, Merrill Lynch was under a duty to timely disclose the reasonably likely decline in the rate of such growth and its loss exposure as affected by the Baldwin debacle.

32. The failure of Merrill Lynch to disclose one or more of the material facts hereinabove alleged was either deliberate or done with reckless disregard for the consequences to plaintiff and other shareholders of Merrill Lynch similarly situated who purchased their Merrill Lynch shares within the class period and to the investing public.

33. The failure of Merrill Lynch to disclose the material facts above set forth caused the price of Merrill Lynch shares in the public market place to be artificially inflated and caused the common stock of Merrill Lynch to be

purchased by the plaintiff and the members of the class at prices far in excess of those at which Merrill Lynch common stock would have been selling had the true material facts been disclosed.

34. The true state of affairs in Merrill Lynch with respect to its liability and financial exposure in Baldwin and Baldwin Insurance Subsidiaries was not disclosed to the purchasers of Merrill Lynch securities during the class period. The potentially adverse impact on the value of Merrill Lynch securities which would have resulted if there had been proper disclosure of all material facts was concealed by defendants until on or about January 24, 1984, when Merrill Lynch announced a $42,000,000 loss for the fourth quarter 1983. It was then stated that a $154,000,000 pre-tax charge was being

taken as a result of the Baldwin United situation. $88,000,000 of the $154,000,000 was stated to be used to pay Merrill Lynch's customers who purchased Baldin SPDAs. The balance was attributed to setting up reserves for money owed by Baldwin to Merrill Lynch.

35. The problems faced by Merrill Lynch, as affected by Baldwin and the Baldwin Insurance Subsidiaries during the class period could not have been ascertained by plaintiff and other purchasers similarly situated with reasonable diligence, until, at the earliest, on or about September 27, 1983, at which time it was announced that an investor had sued Merrill Lynch concerning a Baldwin SPDA he bought through Merrill Lynch alleging that Merrill Lynch had violated securities laws and knowingly concealed knowledge

of Baldwin's worsening financial condition.

36. Defendants knew or should have known that the investment decision of the plaintiff, among other public purchasers of Merrill Lynch would be materially affected by the announcements of defendants and the market climate created for Merrill Lynch.

37. During the class period, plaintiff and other class members purchased Merrill Lynch common stock. In making their purchases, plaintiff and other members of the class relied upon the business and financial information in and disclosed by the reports and statements issued by Merrill Lynch as well as the integrity of the market and the market climate Merrill Lynch created for its common stock.

38. Throughout the class period, the price of Merrill Lynch's publicly traded common stock declined from a high of approximately $96.50 per share on April 26, 1983, which, adjusted for the two for one stock split in June, 1983, would equate to $48.25, to a low of $38.25 on September 26, 1983. Merrill Lynch stock presently trades in the area of approximately $23 3/4 per share. On September 27, 1983 it was publicly disclosed that Merrill Lynch had been sued with respect to its sales of Baldwin annuities. (Exhibit "3", annexed). The price of Merrill Lynch stock immediately declined by nearly ten percent at the close of trading on September 27, 1983. It fell $1.25 per share upon its announcement of January 24, 1984 that it was setting aside some $154 million, $88 million as partial reimbursement for its customers who

bought Baldwin's SPDAs and $66 million as a reserve for money owed to Merrill Lynch in connection with its sale of a subsidiary to Baldwin.

39. As a result of the wrongful acts and material omissions complained of, which continued throughout the class period, shares of Merrill Lynch were purchased by the plaintiff and other shareholders similarly situated at artificially inflated prices and in a false market climate created by defendants.

40. As a result of defendants' wrongful acts and material omissions complained of, plaintiff and other shareholders of Merrill Lynch similarly situated suffered substantial losses on their Merrill Lynch shares purchased in the period complained of and were

damaged thereby in an exact amount presently unknown to plaintiff.

41. The sources of plaintiff's information include but are not limited to the complaint filed in an action entitled Factor v. Merrill Lynch & Co., Inc., et al., USDC SDNY (83 Civ. 7009-CSH), (Exhibit "4", annexed), the reports of Merrill Lynch for the first two quarters of 1983 (Exhibits "1" and "2"), Wall Street Journal articles dated 9/27/83, 9/28/83 and 4/26/83 (Exhibits "3", "5" and "6", annexed), New York Times article dated 4/26/84 (Exhibit "7", annexed), and Business Week articles dated 2/6/84 and 4/9/84, Exhibits "8" and "9", annexed); the grounds of plaintiff's belief are analyses made thereof by his attorneys.

WHEREFORE, plaintiff prays judgment:

(1) That defendants be jointly and severally directed to account and pay to the class of Merrill Lynch shareholders their damages, directly or indirectly resulting from the wrongs alleged herein.

(2) That the Court determine that this action be maintained as a class action, pursuant to Rule 23 of the Federal Rules of Civil Procedure, and that the class be determined to consist of the shareholders of Merrill Lynch who purchased their shares in the period complained of.

(3) That the Court award plaintiff reasonable attorneys' and accountants' fees and expenses, interest, costs and the disbursements of this action.

(4) That the Court grant plaintiff such other, further or different relief as to the Court seems just.

Dated: New York, New York
August 15, 1984

STULL, STULL & BRODY
Attorneys for Plaintiff

By: _____
A Member of the Firm
6 East 45th Street
New York, New York 10017

(212) 687-7230

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

----------x

MICHAEL CEASAR,

Plaintiff-Appellant,

v.

MERRILL LYNCH & CO., INC., et al.,

Defendants-Appellees.

----------x

84-9015

NOTICE OF MOTION

For Expansion of Record or To Have This Court Take Judicial Notice of Documents Filed In Related Proceedings

MOTION BY: STULL, STULL & BRODY
6 East 45th Street
New York, New York 10017
Of Counsel: ROBERT A. STULL
(212) 687-7230

OPPOSING COUNSEL: ROGERS & WELLS, ESQS.
260 Park Avenue
New York, New York 10166
Of Counsel: LOUISE SOMMERS, ESQ.
(212) 878-8000

Has consent of opposing counsel:

A. been sought? x Yes ___ No

B. been obtained? ___ Yes x No

Has service been effected? x Yes ___ No

Is oral argument desired? x Yes ___ No

(Substantive Motions Only)

Requested return date: April 4, 1985
or earlier

(See Second Circuit Rule 27(b))

Has argument date of appeal been set:

A. by scheduling order? ___Yes ___No

B. by firm date of argument notice? _x_Yes ___No

C. If Yes, enter date: April 4, 1985.

Judge or agency whose order is being appealed:

HON. LEONARD D. WEXLER, UNITED STATES DISTRICT JUDGE, EASTERN DISTRICT OF NEW YORK

Brief statement of the relief requested:

Appellant seeks to expand record to including in Joint Appendix four (4) documents (3) filed in two (2) District Courts subsequent to the filing of the Notice of Appeal herein or alternatively to have this Court take judicial notice of the facts contained in such documents.

By: (Signature of Attorney)

ROBERT A. STULL

Appearing for: (Name of Party)

MICHAEL CEASAR -- Plaintiff

-- ORDER --

IT IS HEREBY ORDERED that the motion be and it hereby is granted denied.

IRVING R. KAUFMAN

Seal: United States Court of Appeals
Filed March 25, 1985
Elaine B. Goldsmith, Clerk
Second Circuit

3/25/85

Previous requests for similar relief and disposition:

Motion to Remand to District Court for Consideration of Documents Received Since Appeal and to Expand Record. Motion withdrawn after conference with Staff Counsel. Rule 60(b) motion then made in District Court. Motion denied per Order Wexler, J., dated March 8, 1985.

Statement of the issue(s) presented by this motion:

(1) Whether the Joint Appendix should be either expanded to include on this appeal: (a) Notice of Intent to Issue an Adjudicatory Order and of Respondents' Right to Hearing, issued by the State of Ohio, Department of Insurance; (b) Examiner's Statement of

Investigation, issued to the Bankruptcy Court for the Southern District of Ohio, Western Division; (c) Memorandum of the Amici States, filed in the United States District Court, Southern District of New York in M21-35 (CLB); and (d) Motion of the State of Maine, as Amicus Curiae, filed in M 21-35 (CLB); or alternatively

(2) Whether this Court will take judicial notice of the foregoing documents.

Brief statement of the facts (with page references to the moving papers):

Plaintiff-appellant has appealed from orders of the District Court (E.D. N.Y., Leonard D. Wexler, D.J.) which granted appellees' summary judgment, dismissed the action and denied discovery to appellant. A motion, made by appellees under Rules 9(b) and 12(b), was converted

into a motion for summary judgment by the District Court (p. 2).* Appellant seeks to expand the record to include four documents which first surfaced after the Notice of Appeal was filed (pp. 2-3). The District Court, following dismissal of the complaint, denied appellant's Rule 60(b) motion to expand the record on appeal to include the four documents now sought to be brought to the attention of this Court. This motion is made in the alternative to alert the Court and appellees' counsel that appellant will request this Court to take judicial notice of the facts contained in the four documents described in paragraphs 3 and 5 of the moving affidavit.

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* References are to the pages of the moving affidavit of Robert A. Stull, verified March 19, 1985.

Summary of the argument (with page references to the moving papers):

The dismissal of appellant's class action brought pursuant to §10(b) of the Exchange Act and denial of discovery is the subject of the pending appeal. Judicial or quasi-judicial documents which support the charges of appellant's complaint (p. 4), charge Merrill Lynch with knowledge of similar wrongs as were alleged by appellant in his complaint, and refute the basis of the District Court's dismissal, and which documents first came into existence after the orders dismissing the action, should, in the interests of justice, either be made part of the Record on Appeal, or this Court should take judicial notice of the facts recited therein (pp. 1, 4; Fed. Rules Evid., Rule 201).

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
----------x

MICHAEL CEASAR,

Plaintiff-Appellant,

v.

MERRILL LYNCH & CO., INC.,

Defendants-Appellees

Doc. No. 84-9015

AFFIDAVIT

----------x

STATE OF NEW YORK)
SS.:
COUNTY OF NEW YORK)

ROBERT A. STULL, being duly sworn, deposes and says:

1. I am of counsel to Stull, Stull & Brody, attorneys for plaintiff-appellant herein. I make this affidavit in support of appellant's motion to either (1) enlarge the record on this pending appeal to include as part of the Joint Appendix of the parties four publicly

filed documents which appeared after the Notice of Appeal was filed, or (2) to have this Court take judicial notice of such documents. The documents have been filed in either judicial or quasi-judicial proceedings and refer to the conduct and knowledge of the wrongs alleged in the complaint by one of the appellees, Merrill Lynch & Co., Inc. ("Merrill Lynch").

AFFIDAVIT OF ROBERT STULL - PAGE 2

BACKGROUND

2. Plaintiff-appellant commenced this action by the filing of the complaint on February 1, 1984. The action was brought against Merrill Lynch and three of its officers and directors for violation of Section 10(b) of the Exchange Act. The action was brought as a class action. Defendants-appellees moved to dismiss pursuant to Rules 9(b) and 12(b). The motion was converted into a motion for summary judgment by the Court below which thereafter granted summary judgment and dismissed the complaint. Discovery, duly sought to oppose the summary judgment motion was denied and none has been had. The orders (2) dismissing the action characterized the complaint as pleading

AFFIDAVIT OF ROBERT STULL - PAGE 2

"fraud by hindsight". Notice of Appeal was duly filed on December 10, 1984.

3. By Notice of Motion, dated January 28, 1985, appellant duly moved in this Court for "Remand to District Court for Consideration of Documents Received Since Appeal & to Expand Record". This motion was based upon two documents which first came into being after the District Court's orders appealed from were made. The first document (Exhibit "1", annexed) was a "NOTICE OF INTENT TO ISSUE AN ADJUDICATORY

AFFIDAVIT OF ROBERT STULL - PAGE 3

ORDER AND OF RESPONDENTS' RIGHT TO HEARING" made by the State of Ohio Department of Insurance, under date of December 6, 1984. The second document (Exhibit "2", annexed) was an "EXAMINER'S STATEMENT OF INVESTIGATION" made by an Examiner appointed by the United States Bankruptcy Court for the Southern District of Ohio, Western Division and filed therein. The Court is respectfully referred to pages 3, 6-13, 16-18, 19-21 and 26-29 of Exhibit "1" and pages 88-91 of Exhibit "2".

4. Following conference with Staff Counsel of this Court, the then pending motion to remand and expand the record was withdrawn and appellant duly brought on a Rule 60(b) motion in the District Court seeking to have that Court expand the record to include both the proceed-

ing brought by the Ohio Insurance Department, the Examiner's report and additional documents.

5. At the time the Rule 60(b) motion was made, two additional documents had come to the attention of appellant's counsel and they were sought to be included in the record, as well. These documents are a motion, dated February 6, 1985, made by the State of Maine seeking to appear as amicus curiae in order to oppose a proposed class action settlement in related litigation pending in the United States District Court for the Southern District of New York, M 21-35 (CLB)

and a Memorandum submitted by the Attorney's General of some 20 States, dated February 6, 1985, also in opposition to the proposed class action settlement. Appellee Merrill Lynch was a defendant in those proceedings and charged with knowledge of similar wrongs as were alleged by appellant in his complaint. The Court is respectfully referred to pages 4 and 7-13 of Exhibit "3" and pages 6-15, 21 and 27-36 of Exhibit "4".

REASONS FOR THIS MOTION

6. By Order dated February 8, 1985, the Court below denied plaintiff's Rule 60(b) motion; it declined to request this Court to remand this case, and, it held that plaintiff could not

seek relief from the judgment because the Court lacked jurisdiction to rule upon it. The Court went on to state that it "would be inclined to deny such motion if it had jurisdiction to rule upon it". A copy of such order is annexed as Exhibit "5".

7. Exhibits "1" through "4", above described, support plaintiff's complaint and refute the "fraud by hindsight" theory of the two orders appealed from. Such documents not

only support the charges of plaintiff's complaint, but they show beyond any doubt defendants' awareness of the wrongs pleaded in the complaint at and prior to the times complained of.

8. Appellant is proceeding by motion at this time so that the Court and counsel for appellees will be apprised that appellant will seek to have the four documents above described either made part of the record or will request the Court to take judicial notice of the facts contained therein and so that appellees may not claim surprise upon the argument of the appeal, now scheduled to be heard on April 4, 1985.

_____

ROBERT A. STULL

Sworn to before me this
19th day of March, 1985.

AFFIDAVIT OF ROBERT STULL - PAGE 5

_____
Susan A. Zingalli
Notary Public, State of New York
No. 24-4637844
Qualified in Kings County
Commission Expires March 30, 1986

EXHIBIT 1-PAGE 1

[Letterhead of: State of Ohio Department of Insurance, 2100 Stella Court, Columbus, Ohio 43215]

January 9, 1985

Richard J. Stull, Esq.
Stull, Stull & Brody
6 East 45th Street
New York, New York 10017

Re: Merrill Lynch Life Agency of Ohio, Inc., et al., File No. 84-12-001

Dear Mr. Stull:

I have received your letter dated December 31, 1984. Enclosed please find a copy of the Notice of Intent to Issue an Adjudacatory Order and of Respondents' Right to Hearing in the above-mentioned matter. Please note that Exhibit 'C' to the Notice is deleted due to alleged confidentiality. Counsel for the named Respondents filed a request for Hearing with this Department on January 4, 1985.

EXHIBIT 1-CONTINUED

Due to the claims of confidentiality by Respondents, I am not now at liberty to release any documents received pursuant to our discovery requests. I will retain your letter and let you know if, and when, we may be in a position to provide further information.

Very truly yours,

Deborah J. Kaurich
Attorney
DJK/slc

EXHIBIT 1-PAGE 2

WILLARD W. PIERCE :
c/o Merrill Lynch & Co., Inc. :
One Liberty Plaza :
165 Broadway :
New York, New York 10006 :
:
and :
:
LOUIS C. WARD :
c/o Merrill Lynch, Pierce, :
Fenner & Smith, Inc. :
25 Broadway :
New York, New York 10004 :
:
and :
:
DANIEL M. PERKINS :
c/o Merrill Lynch Life Agency, :
Inc. of New York :
25 Broadway :
New York, New York 10004 :
:
Respondents. :

NOTICE OF INTENT TO ISSUE AN ADJUDICATORY ORDER AND OF RESPONDENTS' RIGHT TO HEARING

1. The superintendent of insurance intends, unless Respondents request a hearing pursuant to Chapter 119 of the Ohio Revised Code, to issue an adjudicatory order: (i) pursuant to Ohio Revised Code Section 3901.22 revoking

EXHIBIT 1-PAGE 2

the life insurance agent's license of Merrill Lynch Life Agency, Inc., of Ohio; (ii) pursuant to Ohio Revised Code Section 3901.22 directing all Respondents to cease and desist from engaging in the types of activities and unfair and deceptive practices described in the charges set forth below in this notice; (iii) pursuant to Ohio Revised Code Section 3901.22 prohibiting indefinitely an insurance company or agency, from employing or permitting Robert C. McClanahan, Gregory F. Fitz-Gerald, Willard W. Pierce, Louis C. Ward, and Daniel M. Perkins to serve as a director, consultant, or in any other capacity; and (iv) taking any other actions permitted by law.

EXHIBIT 1-PAGE 3

2. The foregoing proposed action is based on the charges set forth below which arise out of an investigation conducted by the superintendent of insurance regarding the activities and practices of Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch Life Agency, Inc. of New York, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch & Co., Inc., and the officers and employees of such corporations in connection with the solicitation and sale of single premium deferred annuities (hereinafter "SPDAs") issued by University Life Insurance Co. (hereinafter "University Life"). Discovery in this case may result in additional or amended charges.

3. The superintendent of insurance is charged with the responsibility of licensure of insurance agents pursu-

ant to Ohio Revised Code Chapter 3905, of determining whether violations of Title 39 of the Ohio Revised Code have occurred, and of imposing the appropriate sanctions on such violators as authorized pursuant to Title 39 of the Ohio Revised Code.

4. Ohio Revised Code Section 3901.20 prohibits any person from engaging in an unfair and deceptive act or practice in the business of insurance.

5. Ohio Revised Code Section 3901.21 and Ohio Administrative Code Section 3901-1-06 define unfair and deceptive acts or practices in the business of insurance.

6. Ohio Revised Code Section 3905.21 prohibits any person who is not licensed pursuant to Ohio Revised Code Section 3905.18 from negotiating

EXHIBIT 1-PAGE 3

for, receiving or transmitting any application for an annuity.

EXHIBIT 1-PAGE 6

CHARGE I.

21. The statements contained in paragraphs 1 through 20 of this Notice are incorporated as if fully restated herein.

22. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York, and Merrill Lynch & Co., Inc. issued and distributed to customers and potential customers brochures and materials, including, but not limited to those attached hereto as Exhibits A and B, which brochures and materials contained statements which were untrue, deceptive and misleading, and which misrepresented the benefits and advantages of the SPDAs written by University Life, including but not limited to, the

EXHIBIT 1-PAGE 6

following statements:

(a) "Our SPDAs are virtually risk free";

(b) "Our SPDAs are safe -- backed by preferred stocks and bonds, 85% 'A' rated or better";

(c) "We currently have $1 billion in cash (C.D.s, Treasury Bills) to meet any policy holder's liquidity needs."

(d) "Baldwin insurance companies selling SPDAs have an investment portfolio with a market value of approximately $3.2 billion."

(e) "If every SPDA holder were to request payment tomorrow, Baldwin's insurance companies have sufficient readily marketable investments to pay out 100¢ on the dollar in cash."

(f) "The worst you can do is double your money in nine years time! Baldwin's insurance companies guarantee it";

(g) "Baldwin's insurance companies guarantee these earnings rates for a full year";

EXHIBIT 1-PAGE 7

(h) "Even if the bottom dropped out of everything, the Company guarantees that it will pay at least 7.5 percent a year".

23. The statements set forth in paragraph 22 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(A) and (B).

CHARGE II

24. The statements contained in paragraphs 1 through 23 of this Notice are incorporated as if fully restated herein.

25. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York and Merrill Lynch & Co., Inc. prepared with the intent to use, materials, including but not limited to the materials attached hereto as Exhibit C and entitled "The Ironclad Contract", which materials

EXHIBIT 1-PAGE 7

were untrue, deceptive, and misleading, and which misrepresented the benefits and advantages of the SPDAs issued by University Life, including, but not limited to, the following statements:

(a) "An annuity has so many guarantees you could think of it as the ironclad contract."

(b) "[T]he annuity can help more individuals amass capital in a safe, lower risk manner than many other Merrill Lynch products."

(c) "The company guarantees that if it ever offers you less than 13.5 percent return on your money, you can say 'no thanks', cash in your contract, and there will be no surrender charge."

(d) "Even if the bottom dropped out of everything, the company guarantees that it will pay at least 7.5 percent a year."

EXHIBIT 1-PAGE 8

(e) "10 percent is the amount of your accumulated funds that you can remove in any given year without charge."

(f) "[U]ntil you remove a total equalling your initial deposit, your partial withdrawal is also tax free..."

(g) "You will never get less than your original deposit."

(h) "Guaranteed interest rates"

(i) "Guaranteed tax deferral"

(j) "Guaranteed income for at least as long as you live, if you want it"

(k) "Guaranteed return of principal during the accumulation phase."

(l) "Guaranteed return of principal during the payment phase, if you choose"

(m) "Guaranteed no market risk".

26. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner, & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York and Merrill Lynch & Co., Inc., by and through their agents, made

the statements set forth in paragraph 25 above to customers and potential customers.

27. The statements and activities set forth in paragraphs 25 through 26 above constitute a violation of Ohio Revised Code Sections 3901.20 and 3901.21(A) and (B).

CHARGE III.

28. The statements contained in paragraphs 1 through 27 of this Notice are incorporated as if fully restated herein.

EXHIBIT 1-PAGE 9

29. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York, and Merrill Lynch & Co., Inc. purchased and caused to be published advertisements in newspapers, including, but not limited to the Cleveland Plain Dealer and the Cincinnati Enquirer, (a copy of one such advertisement is attached hereto as Exhibit D) which advertisements contained statements which were untrue, deceptive and misleading, and which represented the benefits and advantages of SPDAs issued by University Life, including but not limited to, the following statements:

(a) "Guaranteed interest rates -- you get a lifetime interest rate guarantee";

(b) "It guarantees the return of your original principal...";

EXHIBIT 1-PAGE 9

(c) "It is available exclusively through Merrill Lynch Life Agency, Inc.";

(d) "Liquidity -- you can withdraw all or part of your money at any time;

(e) "Let Merrill Lynch show how $25,000 can grow to $316,750 (minimum guarantee $81,059)*"

30. The statements set forth in paragraph 29 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(A) and (B).

CHARGE IV.

31. The statements contained in paragraphs 1 through 30 of this Notice are incorporated as if fully restated herein.

32. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of

EXHIBIT 1-PAGE 10

New York, and Merrill Lynch & Co., Inc. circulated materials, copies of which are attached hereto as Exhibits A through C, which contained false, misleading and deceptive statements concerning the financial condition of University Life, and which made reference to the financial condition of University Life's parent corporation and affiliates without an explanation that these companies are not the life insurance company whose product is for sale, including but not limited to the following statements:

(a) "If every SPDA holder were to request payment tomorrow, Baldwin's insurance companies have sufficient readily marketable investments to pay out 100¢ on the dollar in cash."

(b) "Baldwin insurance companies selling SPDAs have an investment portfolio with a market value of approximately $3.2 billion."

EXHIBIT 1-PAGE 10

(c) "We [Baldwin] currently have $1 billion in cash (C.D.s, Treasury Bills) to meet any policy holder's liquidity needs."

33. The statements contained in paragraph 32 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(A),(B) and (D), and Ohio Administrative Code Section 3901-1-06 (D)(16).

CHARGE V.

34. The statements contained in paragraphs 1 through 33 of this Notice are incorporated as if fully restated herein.

35. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of

EXHIBIT 1-PAGE 11

New York, and Merrill Lynch & Co., by and through their agents, made untrue, deceptive and misleading oral statements and oral statements which misrepresented the financial condition of University Life for the purpose of inducing purchasers to refrain from redeeming their SPDAs, including, but not limited to, statements similar to the following:

(a) You should not believe everything you read because the articles which question the financial stability of Baldwin United are written to sell magazines;

(b) I question the credibility of the newspaper articles relative to Baldwin United's financial problems;

(c) The problems reported in the press are of other Baldwin United Companies, not University Life;

(d) The investment in University Life SPDAs is 100% secure;

(e) The investment in University Life SPDAs is fully protected by a state guaranty fund.

EXHIBIT 1-PAGE 11

36. The statements contained in paragraph 35 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(A),(B) and (D).

CHARGE VI.

37. The statements contained in paragraphs 1 through 36 of this Notice are incorporated as if fully restated herein.

38. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York, and Merrill Lynch & Co., Inc. by and through their

EXHIBIT 1-PAGE 12

agents made statements concerning state guaranty funds and the legal reserve system upon which life insurance companies operate, including, but not limited to, statements similar to the following:

(a) No legal reserve company has ever defaulted on a single payment;

(b) Your investment is fully protected by the legal reserve system. It's safer than a bank;

(c) Your money is fully protected by state guaranty funds.

39. The statements contained in paragraph 38 above constitutes violations of Ohio Revised Code Sections 3901.20 and 3901.21(A).

CHARGE VII.

40. The statements contained in paragraphs 1 through 39 of this Notice are incorporated as if fully restated herein.

41. Merrill Lynch Life Agency, Inc.

EXHIBIT 1-PAGE 12

of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York, and Merrill Lynch & Co., Inc. made statements which incompletely compared SPDAs issued by University Life with other investments, including, but not limited to, certificates of deposit, money market funds, bonds, stocks, and treasury bills, for the purpose of inducing, and which tended to induce, customers and potential customers to purchase SPDAs issued by University Life.

EXHIBIT 1-PAGE 13

42. The statements described in paragraph 41 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(A) and (B).

CHARGE VIII.

43. The statements contained in paragraphs 1 through 42 of this Notice are incorporated as if fully restated herein.

44. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, of New York, and Merrill Lynch & Co., Inc. issued and circulated materials, including, but not limited to those materials attached hereto as Exhibits A & B, which contained statements to the effect of "There is no administrative fee" and "There is no sales charge" in connection with the sale of SPDAs issued by University Life.

EXHIBIT 1-PAGE 13

45. Said statements led customers to believe the agent was paid no commission, fee or compensation on the sale of SPDAs issued by University Life.

46. Merrill Lynch Life Agency, Inc. of Ohio and its individual agents were paid commissions, fees and compensation by University Life in connection with the sale of SPDAs.

47. The statements set forth in paragraphs 44 through 46 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(B).

EXHIBIT 1-PAGE 16

CHARGE XI.

61. The statements contained in paragraphs 1 through 60 of this Notice are incorporated as if fully restated herein.

62. On August 1, 1980, Merrill Lynch Life Agency, Inc. of Ohio entered into a sales agreement with University Life pursuant to which Merrill Lynch Life Agency, Inc. of Ohio agreed to promote, market and sell SPDAs issued by University Life.

63. Said sales agreement prohibited Merrill Lynch Life Agency, Inc. of Ohio from encouraging, nor permitting any of its sales force to encourage, the termination, surrender, or cancellation of any SPDA sold pursuant to the agreement during the term of the agreement or for a period of twelve (12) months following a termination of the agreement for certain

reasons set forth.

64. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York, and Merrill Lynch & Co., Inc. by and through their individual agents, advised customers not to cash or surrender their University Life SPDAs and did not disclose to such customers the provisions set forth in paragraph 63 above.

65. Failure to disclose to customers the provision set forth in paragraph 63 above constitutes a violation of Ohio Revised Code Section 3901.20.

CHARGE XII.

66. The statements contained in paragraphs 1 through 65 and of this Notice are incorporated as if fully restated herein.

EXHIBIT 1-PAGE 17

67. Pursuant to the sales agreement between University Life and Merrill Lynch Life Agency, Inc. of Ohio, University Life agreed to pay to Merrill Lynch Life Agency, Inc. of Ohio a sales commission equal to four percent on each University Life SPDA sold by Merrill Lynch Life Agency, Inc. of Ohio; plus an additional one and one-half percent in consideration of promotion, marketing and other services provided by Merrill Lynch Life Agency, Inc. of Ohio payable as follows: (i) 1% upon issuance of the SPDA certificate, and (ii) 1/2% after the SPDA certificate has remained in force for twelve months; plus an additional amount up to one-fourth percent to reimburse Merrill Lynch Life Agency, Inc. of Ohio for all costs incurred specifically in relation to the marketing of University Life SPDAs.

EXHIBIT 1-PAGE 17

68. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York, and Merrill Lynch & Co., Inc. did not disclose, nor did it require individual agents to disclose that said commission was higher than that commonly paid on transactions involving the sale of other securities products.

69. Said failure to disclose the comparative size of commissions paid on University Life SPDAs to customers and potential customers constitutes a violation of Ohio Revised Code Section 3901.20.

EXHIBIT 1-PAGE 18

CHARGE XIII.

70. The statements contained in paragraphs 1 through 69 of this Notice are incorporated as if fully restated herein.

71. Pursuant to said sales agreement, Merrill Lynch Life Agency, Inc. of Ohio was required to reimburse or refund to University Life the commission and fee paid to Merrill Lynch Life Agency, Inc. of Ohio on any SPDA terminated for reasons not attributable to University Life as follows: (i) 100% of the commission and fee on any SPDA terminated during the first six months from the date of issurance; and (ii) 50% of the commission and fee on any SPDA terminated during the second six months from the date of issuance.

72. Pursuant to said sales agreement, 1/2% of the commission and fee

set forth in paragraph 67 above was paid to Merrill Lynch Life Agency, Inc. of Ohio only after the SPDA had remained in force for twelve (12) months.

73. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch & Co., Inc., and Merrill Lynch Life Agency, Inc. of New York, by and through their individual agents, advised customers not to cash or surrender their University Life SPDAs and did not disclose to such customers the provisions set forth in paragraphs 71 and 72 above.

74. Failure to disclose to customers the provision set forth in paragraphs 71 and 72 above constitutes a violation of Ohio Revised Code Section 3901.20.

EXHIBIT 1-PAGE 19

CHARGE XIV.

75. The statements contained in paragraphs 1 through 74 of this Notice are incorporated as if fully restated herein.

76. From December, 1981 through February, 1982, Merrill Lynch White Weld Capital Markets Group, a division of Merrill Lynch, Pierce, Fenner & Smith, Inc., served as a financial advisor to Baldwin-United Corporation, the parent of University Life, in its acquisition of MGIC Investment Corporation, and was compenstated for such services.

77. As of March 24, 1983, Merrill Lynch, Pierce, Fenner & Smith, Inc. owned 350,000 shares of Class A Cumulative Preferred Stock of Thirty B-U Corporations, a subsidiary of D.H. Baldwin Co., which was also a Baldwin-United Corporation subsidiary.

EXHIBIT 1-PAGE 19

78. Merrill Lynch, Pierce, Fenner & Smith, Inc. held a five-year deferred payment note of D.H. Baldwin Co. having a face value amount at maturity on January 1, 1987 of $55,143,000.

79. As of December 31, 1982, Merrill Lynch, Pierce, Fenner & Smith, Inc. carried the note described in paragraph 78 above on its books at a discounted value of $30,761,000.

80. Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch Life Agency, Inc. of New York, Merrill Lynch, Pierce, Fenner & Smith, Inc. and Merrill Lynch & Co., Inc. failed to disclose or require their individual agents to disclose to their customers and potential customers the activities set forth in paragraphs 76 through 79 above.

EXHIBIT 1-PAGE 20

81. The failure to disclose said activities constitutes a violation of Ohio Revised Code Section 3901.20.

CHARGE XV.

82. The statements contained in paragraphs 1 through 81 of this Notice are incorporated as if fully restated herein.

83. On or about January 28, 1983, Merrill Lynch Life Agency, Inc. of Ohio, Merrill Lynch Life Agency, Inc. of New York, Merrill Lynch, Pierce, Fenner & Smith, Inc., and Merrill Lynch & Co., Inc. issued a communication which contained the following statement:

> NEWSPAPER ARTICLES IN THE PAST FEW DAYS HAVE FOCUSED ATTENTION ON THE BALDWIN-UNITED GROUP OF COMPANIES, INCLUDING THE INSURANCE SUBSIDIARIES SELLING SINGLE PREMIUM DEFERRED ANNUITIES. A COMPREHENSIVE EXAMINATION REPORT OF THE ARKANSAS INSURANCE COMMISSIONER, RELEASED ON DECEMBER 31, 1982, CONCLUDED THAT THE ASSETS OF THESE INSURANCE COMPANIES

EXHIBIT 1-PAGE 20

"COVER THE CASH VALUES OF THE SPDA'S" ISSUED BY THEM AND THAT THE COMPANIES "HAD A COMBINED SURPLUS OF $114 MILLION" AS OF SEPTEMBER 30, 1982, THE CLOSE OF THE EXAMINATION PERIOD. THAT REPORT HAS BEEN CAREFULLY REVIEWED BY ACTUARIAL CONSULTANTS AND, BASED ON THEIR REVIEW AND THE ARKANSAS COMMISSIONERS' EXAMINATION, THEY CONCLUDE THAT THESE COMPANIES HAVE RESERVED ADEQUATELY FOR THEIR SPDA OBLIGATIONS.

84. Said communication was designed to discourage holders of SPDA's from redeeming their annuities, and was deceptive, misleading, and misrepresented the examiner's report referred to therein.

85. The statement set forth in paragraph 83 above constitutes a violation Ohio Revised Code Section 3901.20 and 3901.21(A) and (B).

EXHIBIT 1-PAGE 21

CHARGE XVI.

86. The statements contained in paragraphs 1 through 85 of this Notice are incorporated as if fully restated herein.

87. On or about May 2, 1983, Merrill Lynch Life AGency, Inc., Merrill Lynch, Pierce, Fenner & Smith, Inc., Merrill Lynch Life Agency, Inc. of New York, and Merrill Lynch & Co., Inc. issued a set of prepared answers to questions concerning the status of University Life SPDAs, and instructed its employees and agents not to amplify or interpret said prepared answers.

88. Said prepared answers were designed to discourage holders of SPDAs from redeeming their annuities by emphasizing the penalties attached

EXHIBIT 1-PAGE 26

100. Merrill Lynch Life Agency, Inc. of Ohio paid commissions in connection with the sale of SPDAs issued by University Life to the unlicensed persons or unappointed agents listed in paragraphs 91, 94 and 97 above, and to others who were not licensed to sell insurance in Ohio or not appointed by University Life;

101. The activities set forth in paragraph 100, above constitute violations of Ohio Revised Code Section 3905.22 and Ohio Administrative Code Section 3901-1-10(H)(3).

CHARGE XXI.

102. The statements contained in paragraphs 1 through 101 of this Notice are incorporated as if fully restated herein.

EXHIBIT 1-PAGE 26

103. The managing or principal agent of Merrill Lynch Life Agency, Inc. of Ohio knew, or should have known of the activities set forth in Charges I through XX of this notice, and has expressly ratified, encouraged and tolerated said activities, and has failed to notify the Ohio Department of Insurance on those occasions where he knew or had reasonable cause to believe such activities were occurring.

104. The activities set forth in paragraph 103 above constitute violations of Ohio Revised Code Section 3901.20 and Ohio Administrative Code Section 3901-1-40(C).

CHARGE XXII.

105. The statments contained in paragraphs 1 through 104 of this Notice are incorporated as if fully restated herein.

EXHIBIT 1-PAGE 27

106. Merrill Lynch, Pierce, Fenner & Smith, Inc. aided and abetted Merrill Lynch Life Agency, Inc. of Ohio in each of the activities set forth in Charges I through XXI of this Notice including but not limited to, as follows:

(a) Merrill Lynch, Pierce Fenner & Smith, Inc. directed, advised, and instructed Merrill Lynch Life Agency Inc. of Ohio to engage in each of the activities set forth in Charges I through XXI above;

(b) Merrill Lynch, Pierce Fenner & Smith, Inc. trained and instructed agents in standard techniques to solicit customers of Merrill Lynch, Pierce, Fenner & Smith, Inc. to purchase SPDAs;

(c) Merrill Lynch, Pierce Fenner & Smith, Inc. shared in the income or profits, directly or indirectly, from the activities of Merrill Lynch Life Agency, Inc. of Ohio described herein;

EXHIBIT 1-PAGE 21

to redemption and minimizing the financial problems of the Baldwin United Companies, and were deceptive and misleading in that they failed to make, among other disclosures, the disclosures set forth in Charges X through XIV above.

89. The activities set forth in paragraphs 87 and 88 above constitute violations of Ohio Revised Code Section 3910.20.

EXHIBIT 1-PAGE 27

(d) Merrill Lynch, Pierce Fenner & Smith, Inc. dominated and controlled Merrill Lynch Life Agency, Inc. of Ohio as evidenced by the following:

(1) Merrill Lynch, Pierce, Fenner & Smith, Inc. and Merrill Lynch Life Agency, Inc. of Ohio shared officers, directors and management employees;

(2) Merrill Lynch, Pierce, Fenner & Smith, Inc. and Merrill Lynch Life Agency, Inc. of Ohio shared corporate offices;

(3) All individual agents including those licensed, unlicensed, and unappointed, who sold University Life SPDAs through Merrill Lynch Life Agency, Inc. of Ohio were account executives with Merrill Lynch, Pierce Fenner & Smith, Inc. and had entered into exclusive contracts with Merrill Lynch, Pierce, Fenner & Smith, Inc.

(4) Commissions earned through the sale of SPDAs were paid to individual agents by and

EXHIBIT 1-PAGE 28

through the Merrill Lynch, Pierce, Fenner & Smith, Inc. compensation system;

(5) The persons solicited for the purpose of selling SPDAs were customers or potential customers of Merrill Lynch, Pierce, Fenner & Smith, Inc.;

(6) The agents failed to disclose to potential customers that they were acting on behalf of Merrill Lynch Life Agency, Inc. of Ohio.

107. The activities set forth in paragraphs 105 and 106 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(K).

CHARGE XXIII.

108. The allegations contained in paragraphs 1 through 107 of this Notice are incorporated as if fully restated herein.

109. Merrill Lynch & Co., Inc. aided and abetted Merrill Lynch

EXHIBIT 1-PAGE 28

Life Agency, Inc. of Ohio, in each of the activities set forth in Charges I through XXI of this Notice, including but not limited to, as follows:

(a) Merrill Lynch & Co., Inc. directed, advised and instructed Merrill Lynch Life Agency, Inc. of Ohio to engage in each of the activities set forth in Charges I through XXI above;

(b) Merrill Lynch & Co., Inc. deominated and controlled Merrill Lynch Life Agency, Inc. of Ohio;

(c) Merrill Lynch & Co., Inc. shared in the income or profits, directly or indirectly from the activities of Merrill Lynch Life Agency, Inc. of Ohio described herein.

110. The activities set forth in paragraphs 108 and 109 above constituted violations of Ohio Revised Code Sections 3901.20 and 3901.21(K).

EXHIBIT 1-PAGE 29

CHARGE XXIV.

111. The statements contained in paragraphs 1 through 110 of this Notice are incorporated as if fully restated herein.

112. Merrill Lynch Life Agency, Inc. of New York aided and abetted Merrill Lynch Life Agency, Inc. of Ohio in each of the activities set forth in Charges I through XXI of this Notice, including but not limited to, as follows:

(a) Merrill Lynch Life Agency, Inc. of New York, directed, advised and instructed Merrill Lynch Life Agency, Inc. of Ohio to engage in each of activities set forth in Charges I through XXI; and

(b) Merrill Lynch Life Agency, Inc. of New York dominated and controlled Merrill Lynch Life Agency, Inc. of Ohio.

EXHIBIT 1-PAGE 29

(c) Merrill Lynch Life Agency, Inc. of New York shared in the income or profits, directly or indirectly, from the activities of Merrill Lynch Life Agency, Inc. of Ohio described herein.

113. The activities set forth in paragraphs 111 and 112 above constitute violations of Ohio Revised Code Sections 3901.20 and 3901.21(K).

EXHIBIT "2"- PAGE 1

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

IN RE:	:	CONSOLIDATED CASE
BALDWIN-UNITED		NO. 1-83-02495
CORPORATION	:	
D.H. BALDWIN COMPANY		Chapter 11
Debtors and	:	EXAMINER'S STATE-
Debtors in		MENT OF INVESTI-
Possession	:	GATION

Now comes David C. Greer as Examiner pursuant to this Court's appointment and files the following as his Statement of Investigation herein:

1. SUMMARY

The policies and management strategies pursued by Baldwin-United Corporation had placed Baldwin-United in a precarious financial position with its assets clustered in highly regulated subsidiaries and its debts clustered in unregulated holding companies. By late 1981 this problem was apparent to any objective financial analyst of the

EXHIBIT "2"- PAGE 1

company's financial records. It dictated a review and restructuring of policies and strategies which did not take place. Instead the same business approaches that precipitated crisis were pursued to collapse.

Corporate causes of action to recover the losses resulting from that collapse exist, in the Examiner's opinion, against Baldwin-United's chief executive officer, Morley P. Thompson Jr., and against Baldwin-United's board members as those positions were held in December of 1981. Further exploration of potential corporate causes of action against Peat, Marwick, Mitchell & Co., Merrill Lynch and MGIC executives for contributing to those losses is justified.

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The analysis in support of these recommendations and the other conclusions and recommendations which I have reached is presented under the following headings:

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While this Statement of Investigation in its results and in its presentation remains my own, the labors that led to it and tested its conclusions were very much a team effort. I am much indebted to my partner Edward H. Siddens, my associate David F. Rudwall and my expert Touche Ross & Co.

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E. Financial Advisors

Financial problems and the failure of management to assess and react to them in an adequate and timely manner led to the collapse of Baldwin-United. Outside advice that impacted on the process of management assessment and reaction should be considered to have a causative role in the collapse. Business advice came not so much from outside accountants and attorneys as it did from other sources.

In the journey through the events of the years under examination the figure of Merrill Lynch appears at a surprising number of way stations in one guise or another. The variety of roles it assumed and the apparent conflicts among some of those roles raises questions which this examination has not answered but which deserve further exploration. Merrill

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Lynch had a financial investment in Baldwin-United that gave it an interest in the company's rise or fall. It also earned significant profits from its role as a broker-seller of the company's SPDA product. It was also involved in evaluating the company's position and prospects for investors in its role as an investment analyst. It had been engaged as the investment banker on the Colorado bank divestiture in 1980, and in 1981 it was engaged to evaluate Empire Savings, Building & Loan Association. It was later engaged in the valuation of escrow assets in Arkansas. It also hired as part of its brokerage business Milliman & Robertson to review NILIC and NIPIC and was aware of the regulatory problems besetting those companies. It was the seller from which Baldwin-United purchased AMIC, the mortgage insurance

company which was acquired only to be divested in connection with the MGIC acquisition. It was engaged to render a fairness opinion and evaluation of the MGIC acquisition itself.

These are too many roles to generate a sensation of comfort. Regardless of the fabrication of "Chinese walls" between one department or another in an

EXHIBIT "2"-PAGE 89

effort to avoid conflicts of interest, there remains a legitimate concern with a situation where the same "independent" entity that is touting the strength of Baldwin stock in the face of negative reports from other analysts and in the face of a striking deterioration of the company's financial condition, is also depriving significant monies from its own investments in the company and its own sales of the company's product. Of the three investment analysts whom Morley Thompson took on as his personal responsibility, Carol Neeves of Merrill Lynch was one. Her enthusiastic buy recommendation on Baldwin-United stock was one of the beacon lights to investors in the second half of 1982 when the Wall Street Journal and others were making dark suggestions as to Baldwin-United's future.

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If Merrill Lynch had emphasized or even acknowledged the negative risks that existed at the time, a declining stock price and a rising rate of SPDA redemptions might have been triggered. Merrill Lynch had an investment interest in Baldwin-United to protect. More disturbing is the fact that it was earning substantial commissions on sales of Baldwin SPDAs. The initial commission on such a sale was augmented by another 1/2% if the annuity remained in effect for a year. On the other hand if an investor redeemed his annuity within six months of the sale Merrill Lynch was required to refund its sales commission in full. Half of the sales commission would have to be refunded if the annuity was redeemed between

EXHIBIT "2"-PAGE 89

six months and one year from the date of purchase.

Whether or not the potential bias and self-interest of Merrill Lynch played any actual role in its evaluation of Baldwin-United, Merrill Lynch was as a result of its relationships in an excellent position to evaluate the company's financial situation, its strengths and weaknesses and its potential for future performance on the eve of the MGIC acquisition. It had studied the company from the perspectives of investor, sales representative and stock analyst, and it had made specific appraisals of portions of the business' assets. When called upon by

EXHIBIT "2"-PAGE 90

Baldwin-United to provide advice and assistance in the MGIC acquisition, it therefore could be expected to peform such services in an objective, insightful and helpful manner.

The fol'owing account is based on Thompson's recollection of events. It has not been fully confirmed in all relevant details by the documents that have thusfar come under observation. If substantiated, it would furnish the basis for a major claim by the company against Merrill Lynch. Kenneth H. Miller of Merrill's Merger and Acquisition Section solicited the representation of Baldwin-United in connection with the MGIC acquisition. The firm was retained to provide assistance and advice in planning and structuring the proposed transaction and to render a fairness

EXHIBIT "2"-PAGE 90

opinion to the Baldwin Board as to whether or not the price to be paid by Baldwin-United for each MGIC common share was a fair price for a buyer to pay.

According to Thompson, Merrill Lynch's undertaking went beyond technical assistance and the rendering of a fairness opinion. After the Baldwin-United Board had given its approval to the acquisition, there was significant risk that the bankers would refuse the necessary financing and that the proposed deal would fall apart. The questions whether Baldwin-United could afford to pay the acquisition cost and how the price would ultimately be paid were generating constant permutations of the Baldwin-United outline of payment sources and concomitant nervousness and resistance on the part of those being called

EXHIBIT "2"-PAGE 90

upon for a bridge loan. Merrill Lynch was asked to lend its prestige and its knowledge of the company to support a demonstration to the bankers that the acquisition was in fact "doable" from Baldwin-United's standpoint. This demonstration took place at a meeting with the bankers on February 19, 1982. The meeting led to approval of the bridge financing and the acquisition closed in early March. Miller was on vacation at the time of this meeting. Merrill Lynch was represented by the chief of its Merger and Acquisition Section and a younger associate who had been intimately involved in the process.

At the crucial meeting Merrill Lynch had a strong financial stake in the question whether or not the acquisition would go forward. Its agreement with Baldwin-United provided a $1

EXHIBIT "2"-PAGE 90

million fee to Merrill Lynch payable only on the condition that the acquisition was consummated. If the acquisition failed to materialize, Merrill Lynch would receive no part of this fee. Self-interest still being the greatest motivating force in human behavior, this arrangement was hardly conducive to an objective opinion as to the ability of Baldwin-United to pay for the acquisition. According to Thompson, Merrill Lynch requested an additional fee for its role at the February 19th meeting with the bankers and for adding the concept of doability to the concept of fairness in its evaluations. Thompson refused to pay the additional fee on the basis that there was more than enough profit in a contingent fee of $1 million to compensate Merrill Lynch for its services. Merrill Lynch took the $1 million.

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An objective financial advisor asked the determinative questions as to the wisdom, practicality, fairness and doability of the MGIC acquisition in late 1981 or early 1982 would, in my opinion, have impressed the Baldwin-United Board and the Baldwin-United bankers with the facts outlined in the financial tables and charts attached as Appendices to this Statement of Investigation. Had either the bankers or the Board been fully aware of those facts and their implications, it is doubtful that the acquisition would have been consummated, and it is probable that there would have been changes of strategy that would have permitted Baldwin-United to remain a viable company. If these assumptions are correct, Merrill Lynch-by letting objectivity yield to self-interest and by permitting itself to be used as a

EXHIBIT "2"-PAGE 90

means of tying down financing for the acquisition-bears a share of the damage that has been done to the Debtors in these proceedings.

EXHIBIT 3- PAGE 1

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

MDL NO. 581 - IN RE BALDWIN-UNITED CORPORATION LITIGATION: M21-35 (CLB)

THIS DOCUMENT RELATES TO THE FOLLOWING ACTIONS:

84 Civ. 0098 (CLB)
84 Civ. 2234 (CLB)
84 Civ. 6575 (CLB)
84 Civ. 1673 (CLB)
83 Civ. 7179 (CLB)
83 Civ. 8084 (CLB)
83 Civ. 8475 (CLB)
83 Civ. 7009 (CLB)
84 Civ. 3084 (CLB)
83 Civ. 7568 (CLB)
84 Civ. 2233 (CLB)
83 Civ. 7358 (CLB)
83 Civ. 8474 (CLB)
83 Civ. 7359 (CLB)
84 Civ. 0407 (CLB)
84 Civ. 7297 (CLB)
84 Civ. 8802 (CLB)
85 Civ. 0279 (CLB)

THIS DOCUMENT SUBMITTED ON BEHALF OF:
THE STATE OF MAINE, AS AMICUS CURIAE

AFFIDAVIT OF PETER J. BRANN
IN OPPOSITION TO PROPOSED
CLASS ACTION SETTLEMENT

EXHIBIT 3-PAGE 4

following the collapse of the insurance subsidiaries of Baldwin that issued the SPDAs (collectively, the "Baldwin Insurance Companies"). Many State Attorneys General have conducted investigations in the Baldwin matter, focusing upon the marketing of Baldwin SPDAs by the nation's major brokerage firms, the Defendants in these proceedings. Often, under the authority of their consumer protection statutes, State Attorneys General issued civil investigative demands or subpoenas to the Defendants to obtain information concerning the Defendants' role in the sale of billions of dollars in Baldwin SPDAs. Additionally, the state insurance regulators and/or the securities regulators in many states conducted investigations, the results

of which in some cases were made available to the State Attorneys General. Maine, for example, in subpoenas issued jointly by the Attorney General, the Superintendent of Insurance, and the Superintendent of Banking, sought and obtained relevant information from all of the brokers -- both large and small --who sold Baldwin annuities in Maine. Many of these brokers are now the Settling Defendants before this Court.

6. In addition to investigations conducted by the States, some States have initiated administrative proceedings or civil litigation relating to the Baldwin matter. In most cases, these proceedings have involved the Settling Defendants.

EXHIBIT 3-PAGE 7

FACTUAL ALLEGATIONS

11. Despite its surface complexity, the relevant facts in this litigation are not complex. The factual allegations may be divided into three categories: (1) the rise and fall of Baldwin and its subsidiaries; (2) the knowledge -- actual or presumed -- of the Defendants concerning the rise and fall of Baldwin and its insurance subsidiaries; and(3) the representations the Defendants made to consumers despite that knowledge.

12. Volumes have been written about the history the Baldwin collapse. The most comprehensive statement to date of the history of Baldwin is the Examiner's Statement of Investigation filed January 15, 1985, in the United States Bankruptcy Court for the

EXHIBIT 3-PAGE 7

Southern District of Ohio, Western Division ("Examiner's Report"). Although the Examiner's Report explicitly states that it is beyond the parameters of that report to consider "the potential claims of SPDAs purchasers for alleged misstatements, overpromotion or nondisclosure in the sale of those products," Examiner's Report at 4, it nevertheless provides the best description of Baldwin's unprecedented and unsafe business practices. A copy of the Examiner's Report is attached hereto and incorporated herein as Exhibit A. The Examiner's Report confirms that Baldwin SPDAs

EXHIBIT 3-PAGE 8

were not risk-free, outstanding investments, and indeed, Baldwin and the Baldwin Insurance Companies were imprudently and dangerously managed.

13. The Defendants knew, or should have known, that Baldwin's business practices in particular were unprecedented and unsafe. Throughout the period that the Defendants marketed Baldwin SPDAs, there was publicly available information that cast doubts on the safety of Baldwin SPDAs. This information was available in financial reports filed with the states of Arkansas and Indiana, Baldwin's public statements, especially those surrounding the december 1981 purchase of MGIC Investment Corporation, articles appearing in the financial press, such as those in the Wall Street Journal,

EXHIBIT 3-PAGE 8

and critical analyses of Baldwin, such as those published by Gilford Securities, Inc. As a result of the publicly available information, the Defendants -- some of the most sophisticated financial advisers in the country -- knew, or should have known, that Baldwin was relatively inexperienced in managing insurance companies, that the Baldwin Insurance Companies were too small and had inadequate reserves to manage billions of dollars of SPDA sales, that Baldwin was using the reserve of its insurance company to finance a dangerous and aggressive acquisition policy, that Baldwin's SPDA business was dependent upon an

EXHIBIT 3-PAGE 9

unprecedented, complicated and unapproved tax strategy, and that Baldwin's corporate strategy generally and its insurance strategies in particular, were risky.

14. In addition to the publicly available information, virtually all of the Defendants had access to material non-public information that confirmed the precarious nature of the Baldwin SPDA empire. For example, many of the Defendants retained the services of Milliman & Robertson, Inc., or other consulting actuaries, to evaluate the financial condition of the Baldwin Insurance Companies. Of course, ignorance is not a defense for those Defendants who took no steps to investigate either the health of the Baldwin Insurance Companies or

EXHIBIT 3-PAGE 9

the truth of the representations concerning Baldwin SPDAs. Typical of the information that was available to all, or virtually all, of the Defendants is the information contained in Exhibits D-K, which are incorporated herein. Because these documents are confidential, they are being filed separately with the Court under seal. Suffice to say, however, each of the Defendants knew, or had reason to know, many of the facts concerning the unsound and risky nature of Baldwin SPDAs including, without limitation, that Baldwin was paying out more in credited interest, commissions, and other expenses than they were collecting in SPDA premiums, that the Baldwin SPDA program was contingent upon a novel and complicated tax strategy subject to

EXHIBIT 3-PAGE 10

IRS disapproval, that the moneys generated by Baldwin SPDA sales were not invested prudently, but rather were used to finance Baldwin's insatiable appetite for growth, and that Baldwin's acquistion strategy threatened the solvency of the Baldwin Insurance Companies.

15. Although the Defendants harbored serious doubts about the Baldwin SPDA program, they marketed Baldwin SPDAs aggressively. The growth in Baldwin in Baldwin SPDA sales is directly related to the relationship between Baldwin and the Defendants. Baldwin used the Defendants to gain respectability and name recognition, and access to the enormous marketing network of the Defendants. Both the Defendants' market research and the

EXHIBIT 3-PAGE 10

States' investigations confirm that the Defendants, meanwhile, used the attractive twin features of Baldwin SPDAs -- complete safety and high yield -- to attract thousands of new customers over the age of 45 who were concerned about risks and retirement income and who had little previous experience in making investments. Additionally, the Defendants received commissions and other administrative charges of between four and five percent of their SPDA sales, a sum substantially in excess of what they could earn selling other products. Finally, Baldwin SPDAs offered "guaranteed" yields substantially in excess of those offered for other SPDAs and for other products generally recognized as safe, such as savings accounts.

EXHIBIT 3-PAGE 11

16. Although the Defendants knew or should have known, that there were substantial risks facing consumers, they nevertheless represented to consumers that Baldwin SPDAs were completely safe, outstanding investments. They typically described Baldwin SPDAs as "money in the bank" or "like buying a government bond." Irrespective of the State or the Defendant, consumers were told by all of the Defendants that Baldwin SPDAs were risk free, high yield investments. Typical of the materials prcvided by the Defendants to consumers were those provided by one Defendant to one Maine consumer, which are attached hereto and incorporated herein as Exhibit B. In addition to the written materials provided by the Defendants to consumers, Defendants

provided other promotional materials which contained similar unequivocal representations concerning Baldwin SPDAs. Typical of such promotional materials is a transcript of a record provided by one Defendant to a consumer outside the State of Maine, which is attached hereto and incorporated herein as Exhibit C. In sum, the representations made by the Defendants were uniform and unequivocal -- and untrue.

17. In addition to the written materials provided directly to consumers, the Defendants provided similar materials to their account representatives, which then were used by the account representatives to make representations to consumers.

EXHIBIT 3-PAGE 12

Typical of the materials provided by each of the Defendants to their respective account representatives are the materials in Exhibit L, which is incorporated herein. Because of the confidential nature of these materials, these materials have been provided separately to the Court under seal. On balance, it is beyond dispute that the Defendants represented Baldwin SPDAs to be completely safe. Likewise, they represented to consumers that Baldwin SPDAs were a no loss proposition in that the guaranteed high yields would not decline, because of market forces, and if they did decline more than 3/4 of one percent, the consumer would be able to obtain his money and accummulated interest. Therefore, the Defendant

EXHIBIT 3-PAGE 12

told consumers they were "guaranteed" that Baldwin SPDAs were completely safe and they would always receive a high interest rate.

18. The Defendants did not have any basis whatsoever for the unqualified and unequivocal representations that Baldwin SPDAs were risk free, high yield investments. Baldwin SPDAs were backed only by the solvency of Baldwin itself, and indeed, was subject to substantial risks, as the Defendants knew, or should have known, and as events have demonstrated only too conclusively.

19. Because the Defendants lacked any basis, and certainly an adequate basis, for their representations concerning the control aspects of Baldwin's SPDAs their actions were deceptive

EXHIBIT 3-PAGE 13

and misleading. Because the misrepresentations concerned the central aspects of Baldwin SPDAs, a substantial number of consumers were deceived in a material respect, a fact confirmed by the States' investigations. Thus, the Defendant committed unfair and deceptive acts and practices in violation of state and consumer protection statutes.

EXHIBIT 4

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

MDL NO. 581 - IN RE BALDWIN- UNITED CORPORATION LITIGATION:	
THIS DOCUMENT RELATES TO THE FOLLOWING ACTIONS:	M21-35 (CLB)
84 Civ. 0098 (CLB)	
84 Civ. 2234 (CLB)	
84 Civ. 6575 (CLB)	
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83 Civ. 7359 (CLB)	
84 Civ. 0407 (CLB)	
84 Civ. 7297 (CLB)	
84 Civ. 8802 (CLB)	
85 Civ. 0279 (CLB)	
THIS DOCUMENT SUBMITTED ON BEHALF OF THE ATTORNEYS GENERAL OF: THE STATES OF MAINE, MASSACHUSETTS, TEXAS, NEW YORK, GEORGIA, ARIZONA, NEW HAMPSHIRE, MISSOURI, NEW MEXICO, WASHINGTON, NORTH DAKOTA, OHIO, ILLINOIS, CALIFORNIA, CONNECTICUT, NEBRASKA, NEVADA, KENTUCKY, MICHIGAN, TENNESSEE, AS AMICI CURIAE	

MEMORANDUM OF THE AMICI STATES IN OPPOSITION TO PROPOSED CLASS ACTION SETTLEMENT

EXHIBIT 4-PAGE 6

By mid-1983, Baldwin's total revenues from the sale of SPDAs exceeded $4 billion. This stunning explosion in SPDA sales can be traced to Baldwin's 1980 development of a new, symbiotic relationship with the major brokerage firms in the country, the Defendants in these multidistrict proceedings.

Baldwin benefitted enormously from their relationship with the Defendants -- the nation's major brokers -- because they provided Baldwin with access to their extensive national marketing network -- that is, access to hundreds of thousands of potential middle-class clients. Moreover, because the Defendants, who had staked their reputations on the value of their investment advice, represented Baldwin SPDAs to be outstanding investments, their participa-

tion also gave Baldwin name recognition and respectability in the world of insurance and finance.

The Defendants benefitted as well. They marketed the Baldwin SPDAs as safe, high-yield investments, a product that enabled them to attract an enormous number of conservative investors who rarely, if ever, had used the service of a securities dealer 3/ As the figures reveal, this marketing strategy was enormously successful, thereby giving the

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3/ According to surveys conducted by the States, as well as market research conducted by the Defendants, Baldwin SPDAs primarily were purchased by older, more conservative people, who either were planning for their retirement or were concerned about risky investments.

Defendants entree to the enormous and lucrative insurance market.

To cement this relationship between Baldwin and the Defendants, Baldwin agreed to pay the Defendants commissions and administrative charges equivalent to four or five percent of the Defendants' SPDA sales. These commissions were substantially higher than the commissions the Defendants could earn selling other products. 4/ This arrangement provided a substantial inducement for the Defendants to market the Baldwin SPDAs aggressively, thus setting the stage for the explosive

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4/ Because the commissions paid to the Defendants were not deducted from the amounts paid by consumers, but instead had to be generated from other sources, this also contributed to Baldwin's subsequent financial difficulties

EXHIBIT 4-PAGE 7

growth in Baldwin's SPDA business.

The final ingredient in the calculus was the product itself --the Baldwin SPDA. Baldwin SPDAs "guaranteed" consumers a high first-year interest of up to 15.5%. Significantly, the promised interest rates were substantially higher than either the rates for SPDAs issued by other insurance companies or the rates for other, recognizably safe investments, such as savings accounts. Baldwin SPDAs further "guaranteed" that if the promised high interest rate ever declined more than 3/4 of one percent, consumers could withdraw their money and accumulated interest without penalty, and invest it in another investment.

EXHIBIT 4-PAGE 8

offering comparable features. In short, Baldwin SPDAs offered to the 160,000 conservative consumers who purchased them the ideal investment -- a completely safe, high-yield investment.

The Baldwin SPDA empire, however, was a corporate house of cards. Prior to marketing the Baldwin SPDAs, many of the Defendants retained the services of Milliman & Robertson, Inc. ("Milliman & Robertson"), consulting actuaries, to evaluate the financial condition of the Baldwin Insurance Companies. Beginning in January 1980, Milliman & Robertson warned the Defendants that the Baldwin SPDA business was contingent upon Baldwin's novel and

unapproved tax scheme. [5/] Additionally, Milliman & Robertson expressed concern about the Baldwin Insurance Companies' inadequate surpluses and reserves to cover the increasingly large number of Baldwin SPDAs being marketed. Finally, the relative inexperience of the former piano company and the inadequate size of its insurance subsidiaries to finance and manage billions of dollars of SPDAs were apparent at the outset even to the most casual observers.

5/ In each report between 1980 and 1983, Milliman & Robertson warned the Defendants that the Baldwin SPDA operation depended in large part upon IRS approval, which was never obtained. On the contrary, following the collapse of the Baldwin empire, the IRS filed a $450 million tax claim in the Baldwin bankruptcy proceedings, which, if asserted against the Baldwin Insurance Companies, would increase the Plaintiff's damages enormously.

EXHIBIT 4-PAGE 9

In addition to the inherent risks known to the Defendants when they began marketing Baldwin SPDAs, another serious risk to the safety of Baldwin's SPDAs -- the Baldwin acquisition policy -- soon became apparent. Ordinarily insurance companies use consumers' insurance premiums to make conservative investments and to finanace reserves. Baldwin, however, used consumers' insurance premiums to make speculative investments and to purchase affiliates and subsidiaries for the Baldwin -- ate empire. In exchange for the marketable assets of the Baldwin Insurance Companies -- moneys paid by consumers and high grade stocks and bonds -- Baldwin substituted the assets of Baldwin affiliates and subsidiaries ("affiliate assets"). Furthermore,

the affiliate assets often were of uncertain value and liquidity since Baldwin arbitrarily valued its own affiliate assets. Baldwin's unprecedented investment strategy was outlined in the financial reports filed with the insurance regulators of Indiana and Arkansas and was reported in the financial press.

The apex of this approach occurred in December 1981 when Baldwin announced that it planned to buy MGIC Investment Corporation ("MGIC") for $1.2 billion completely with internally generated funds. As reported in the Wall Street Journal following the December 17, 1981 announcement:

EXHIBIT 4-PAGE 10

> James Schwab, Treasurer of Baldwin-United, says those annuity proceeds "could be one of the three of four major sources of funds" for the MGIC acquisition. That's what has the accountants perplexed. Ordinarily, most of these proceeds must be held as reserves for future payouts on the insurance policies. And reserves have generally been taken to mean safe, stoggy investments, such as preferred stocks and long-term bonds, rather than acquisition targets. "I don't understand how they can use the reserve funds" to pay for MGIC says Ray Dirks, a long time watcher of insurers' financial statements.

Therefore, by the beginning of 1982, Baldwin's strategy was clear: it would generate substantial income by selling a product, the success of which was dependent upon a novel and unapproved tax strategy, and then it would use the proceeds generated not to fund reserves, but rather

EXHIBIT 4-PAGE 10

to fuel an aggressive acquisition policy.

The risks for Baldwin SPDA policyholders were significant and apparent to the Defendants. Based upon their consultants' reports, Baldwin's financial reports, Baldwin's financial reports, and reports in the financial press, all of the Defendants were aware, or should have been aware, that the Baldwin SPDA strategy was financially unsound. Indeed, on July 13, 1982, one of the Defendants summarized some of the known risks as follows:

> (a) Organization and structure in operations are very complex with tax considerations playing an important role. An article in Fortune Magazine March 8, 1982 quotes a

EXHIBIT 4-PAGE 11

lawyer involved in a Thompson (Chief Executive of Baldwin-United) transaction as complaining of "deals that I can't understand even after extended study." This same article quotes a Wall Street banker as saying "Look, Thompson's smarter than you and me. If he's doing anything wrong, we won't know until it's too late."

(b) Insurance subsidiaries of Baldwin-United have been used, as much as legally permitted, to finance other areas. An example of this is the acquisition of MGIC in March. *** It seems fair to say that Baldwin-United has used its insurance subsidiaries for general corporate purposes as much as possible while staying in the letter of the law.

(c) The parent company, Baldwin-United, is heavily leveraged. The December 31, 1981 shows debt of $753,547,000 in stockholders' equity of $325,668,000.***

(d) Reflecting the above, S & P lowered it debt rating on Baldwin-United to BB from BB+ at the end of April. Commercial Paper of D.H. Baldwin a financial services subsidiary was dropped to A-3 from A-2.

EXHIBIT 4-PAGE 11

The possible impact of these risks upon the Baldwin Insurance Companies was made clear by the further observation in the July 13, 1982 memorandum that: "Most states have an emergency insurance fund to pay policyholders in the event of default but all policyholders would not necessarily be paid in full." Apparently undaunted by such clear signals of ever increasing risks, the Defendants continued to market Baldwin SPDAs aggressively, and, paradoxically, continued to stress, above all else, the safety of Baldwin SPDAs.

EXHIBIT 4-PAGE 12

Throughout the summer of 1982, additional cracks in the Baldwin empire appeared. In August 1982, the Securities Valuation Office of the National Association of Insurance Commissioners evaluated the affiliate assets held by the Baldwin Insurance Companies, which revealed that those values were substantially overstated by the Baldwin Insurance Companies. Accordingly, in August of 1982 it was necessary for Baldwin to inject $210 million into NIPIC to maintain its solvency. These and other problems described above led at least one securities analyist, James Chanos of Guilford Securities, to publish a highly critical -- and publicly available -- analysis of Baldwin and its corporate policies, which concluded that Baldwin "[c]ontinued [its] heavy

reliance on affiliated securities in the insurance portfolios," and that although Baldwin "maintains that they can pay off every [SPDA] sold with cash and marketable securities [w]e do not agree."

Because of the continued deterioration of the Baldwin Insurance Companies' financial condition, it is scarcely surprising that the August 24, 1982 Milliman & Robertson report to the Defendants observed that the "focus of our review is on solvency." After reiterating concerns about the still unapproved tax strategy, the questionable investment policies, and the inadequate reserves, the Milliman & Robertson report

EXHIBIT 4-PAGE 13

starkly outlined the questions confronting the Baldwin Insurance Companies and the Defendants:

> The primary question is not one of whether, during a future period of increasing interest rates, the portfolio will be able to produce adequate yields, the primary question is a more fundamental question and a near-term question. Is the yield of the portfolio in the near-term --even in the absence of investment market fluctuations --specified or certain or predictable?

Although the answers to these questions should have been painfully obvious to the Defendants, they continued to promote and sell Baldwin SPDAs throughout 1982 and into 1983, notwithstanding the financial hemorrhaging of the Baldwin Insurance Companies.

Just as the Defendants ignored Milliman & Robertson's 1980 warning that the Baldin SPDA plan could work

EXHIBIT 4-PAGE 13

"subject to IRS approval," the Defendants ignored Milliman & Robertson's 1982 warnings that the Baldwin SPDA plan could render the Baldwin Insurance Companies insolvent. Moreover, Milliman & Robertson did not sound the only alarm. On the contrary, numerous critical articles, focusing on Baldwin's novel and untested past accounting practices and its risky corporate policies, appeared in the financial press.

In 1983, the financial condition of both Baldwin and its insurance companies continued to decline precipitously. Baldwin's liquidity problems increased as it missed several

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deadlines to repay a $440 million loan in March and April. The Baldwin Insurance Companies' affiliate asset problems also increased, evidenced by Baldwin's March agreement to pay a $100,000 fine in Arkansas due to its over investment in affiliate assets. When Baldwin finally filed its 1982 10-K Report on April 17, 1983, it admitted that it would be out of cash by mid-year if it did not get new financing or sell major assets. It was only at this point that Merrill Lynch, the largest marketer of Baldwin SPDAs, agreed to stop its SPDA sales. On May 2, 1983, the Baldwin Insurance Companies voluntarily suspended all SPDA sales and, on July 13, 1983, Arkansas and Indiana placed the Baldwin

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Insurance Companies in rehabilitation, a proceeding for insurance companies akin to bankruptcy.

Between July 13, 1983 and October 17, 1983, the Arkansas and Indiana insurance commissioners, appointed by their respective state courts to manage the Baldwin Insurance Companies worked to develop a rehabilitation plan. The proposed rehabilitation plan was designed to restructure the Baldwin Insurance Companies, manage the available assets, and provide consumers with whatever available moneys that resulted from the rehabilitation plan. Following hearings in January 1984 limited to the issues surrounding the feasibility of the rehabilitation plan, the Arkansas and Indiana courts approved

the rehabilitation plan, to begin in May 1984 and to continue until November 1987.

Under the terms of the rehabilitation plan, consumers generally are credited with their promised first-year interest, with a 9.5% interest rate between July 13, 1983 and May 1, 1984, and with an "assured" 5.5% interest rate between May 1, 1984 and November 1987. Although consumers were permitted to obtain some of their money beginning in August 1984--up to a 75% "loan" -- they generally were not permitted to receive any of their money between July 13, 1983 and August 1984.

During 1983 and 1984, consumers filed over 90 federal civil actions

against many of the brokers who sold Baldwin SPDAs, as well as Planco, Inc. ("Planco"), a company that assisted the brokers in marketing Baldwin SPDAs (collectively, the "Defendants"). Most of these actions were transferred to this Court by the Judicial Panel on Multi-District Litigation for coordinated or consolidated pre-trial proceedings, pursuant to 28 U.S.C. §1407. After filing consolidated or amended complaints in the Spring of 1984, but before conducting hardly any other pre-trial proceedings, the Plaintiffs entered into virtually identical Stipulations of Settlement ("proposed settlement") with seventeen brokers and Planco (collectively the "Settling Defendants"), which are now before the Court for final approval.

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17. Prior to and during the Class Period, Defendants knew or should have known but for their reckless conduct of the following materially adverse information with regard to Baldwin-United and the Baldwin Insurance Subsidiaries and the SPDAs:

***

(j) In selling the SPDAs Defendants violated state licensing stautes and other state laws.

***

58. At all relevant times there were in effect in many of the states in which defendant solicited or sold SDPAs, laws such as licensing and registration of sellers of SPDAs, and regulations of sales to consumers, which were enacted for the benefit and protection of purchasers of goods or service [sic] and/or which prohibited certain of the activities and transactions of the Defendants alleged herein, and laws which impose statutory standards of fiduciary obligation on the Company.

59. Defendants violated the laws referred to in parargraph 58 by the activities and transactions of defendants herein alleged.

60. As a result of the foregoing, Plaintiffs and the Class have been damaged and Defendants are liable for such damages, recission, punitive

damages, attorneys' fees, and such further relief as is just and proper.

Second Amended Complaint ¶¶ 17(j), 58-60. 9/

9/ In their Consolidated Amended Complaint against Merrill Lynch, in addition to the allegations against all of the other Defendants quoted above, the Plaintiffs also alleged that "Merrill Lynch violated certain state statutes and regulatory requirements by offering SPDAs without being licensed and by unlawfully referring to, and describing inaccurately state insurance guaranty benefits." ¶ 28.

violation of section 5. Misrepresentations are condemned if they possess a tendency to deceive."); Resort Car Rental System, Inc. v. FTC, 518 F.2d 962, 964 (9th Cir.), cert. denied sub nom. MacKenzie v. United States, 423 U.S. 827 (1975) ("Neither actual damage to the public nor actual deception need be shown."). Thus, we need only analyze the misleading or deceptive nature of the representations made by the Defendants directly or indirectly to consumers.

The Defendants made a plethora of representations to consumers concerning Baldwin SPDAs. The promotional materials provided by the Defendants to consumers generally stressed two themes -- first, Baldwin SPDAs were completely safe, secure investments;

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and second, Baldwin SPDAs guaranteed consumers high yields. Some, but by no means all of these representations, include:

> Our SPDAs guarantee you high interest . . . tax deferred.
>
> Our SPDAs funds grow for retirement . . . but you can take money out when you need cash.
>
> Our SPDAs are safe -- backed by preferred stocks and bonds, 85% "A" rated or better.
>
> We currently [in 1982] have $1 billion in cash (CD's, Treasury Bills) to meet any policyholder liquidity needs.
>
> Your money is always available when you need it.
>
> Our SPDAs are virtually risk free.

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Double your money in six to nine years.

At our current yield, your SPDA funds will double in six short years. But consider this. The worst you can do is to double your money in nine years time! Baldwin's Insurance Companies guarantee it. No matter what happens to the prime rate. No matter what the state of the economy.

Here at last is a solid growth opportunity for your money where safety is the key. Because the insurance companies which issue your annuity are rated "A" by A. M. Best -- the industry watchdog. They are also regulated by state insurance departments. Moreover, the portfolio that backs your SPDA is second to none.

Your single premium deferred annuity provides a 100% guarantee of your principal and accumulated interest, net of any distribution charges. You are further guaranteed to receive no less than your full contribution.

Minimum guarantee of 7.5% years two through ten.

Your annuity deposit is guaranteed to more than double in value for

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the first ten years.

You enjoy all the benefits of a tax shelter with the guaranteed safety of a savings account.

This is a high yield shelter with a very attractive rate of return comparable to or even better than the best municipal bonds.

Unlike stocks, even preferred stocks or bonds, you receive all of the advantages of the tax shelter without risking a penny. Your money is as secure as it would be in a savings account.

(Emphasis in original)

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In addition to the written materials provided directly to consumers, the Court also must take into consideration the written materials provided by the Defendants to their account representatives. See Regina Corp. v. FTC, 322 F.2d 765, 768 (3d Cir. 1963) ("One who places in the hands of another a means of consummating a fraud or competing unfairly in violation of the Federal Trade Commission Act is himself guilty of a violation of that Act.") (citations omitted); Standard Distributors, Inc. v. FTC, 211 F.2d 7, 12-13 (2d Cir. 1954) (principal is liable for misrepresentations made by agents in the apparent scope of their authority even though the principal made some efforts to prevent the deceptions).

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The Defendants' training materials also emphasized unequivocally that Baldwin SPDAs were completely safe, high-yield investments:

> The highlights of the National Investors's -- University annuity are as follows: (1) completely safe. No market risk.
>
> It has often been said that if the client is convinced the annuity is as safe as is money in the bank, he'll buy.
>
> "How do I know it's safe?" This question -- as often unspoken as it is spoken -- is usually one of the most important points in any annuity sale. If you have properly targeted the source of the money and the proposed annuity purchase, the client's long term secure dollars, the bank's CD's, the passbook savings accounts, that is being taxed every year, then, the sale ultimately turns on assuring him of the annuity contract's safety, because the client already knows his money is safe in the bank.

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Just like the money market fund, the annuity is very safe, and it costs nothing to buy but it has one great advantage: no current tax on interest earnings.

The key to turning a commission-less money fund into a 4% growth commission annuity is to answer the only objection you'll encounter, "what if I need the money?"

The great attraction of the annuity to the client is the combination of complete safety and tax protection. There is only one safe way in the country today that the client can get rid of its current income taxes year after year on his bank CD, his savings type dollars, his money market fund balances that come from CD and that is the modern annuity -- a better way to pile up money for the future.

In all of these questions the client is really saying, "if you can convince me it's as safe as money in the bank, I'll buy it -- because I can see that tax-wise it's a much better deal."

Stress the safety and generally you will have a sale.

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There can be little doubt that the Defendants unequivocally represented to consumers that Baldwin SPDAs were risk-free, outstanding investments. Investigations conducted by various States confirm that the Defendants routinely represented to consumers that purchasing a Baldwin SPDA was like "putting money in the bank" or "buying a government bond." Moreover, the Defendants represented and the Baldwin SPDA explicitly stated, that if the interst rate ever dropped more than 3/4 of one percent below the high, first-year contract rate, consumers

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could withdraw their entire accumulated value without charge. In short, Baldwin SPDAs were represented to be no-loss propositions. Finally, in making these representations, the Defendants held themselves out as financial experts who had carefully researched all pertinent aspects of these products before arriving at their favorable conclusions.

There can be little doubt that the Defendants' representations had the tendency or capacity to mislead or deceive consumers.[13/] "It is settled law that an advertiser in rendering

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13/ Because these representations concern the central features and attributes of Baldwin SPDAs, they certainly cannot be considered to be mere subjective expressions of opinion or "puffing." See FTC Statement of Basis and Purpose for the Cigarette Rule, 29 Fed.Reg. 8325, 8351 (July 2, 1964) ("While the

an affirmative claim for a product must have a 'reasonable basis' therefor, consisting of such evidence as is appropriate to provide substantiation for the type of claim being made." National Commission on Egg Nutrition, 88 F.T.C. 89, 91 (1976), aff'd as modified, 570 F.2d 157 (7th Cir. 1977), cert. denied, 439 U.S. 821 (1978) (citations omitted);

13/ courts still make occasional reference to the fact-opinion distinction, they recognize no privilege for statements of opinions in advertising, and invariably regard as a deceptive and unlawful representation any opinion stated in such a manner as to mislead the consumer. The traditionally broad scope of permissible 'puffing' has been narrowed to include only expressions that the consumer clearly understands to be pure sales rhetoric on which he should not rely in deciding whether to purchase the seller's product. The test, thus, is not whether a representation is intended as a statement of fact or one of opinion, but whether it is likely to mislead the consumer.") (citation and footnotes omitted)

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see also American Home Products Corp. v. FTC, 695 F.2d at 693 n. 20 (collecting cases). Indeed, in representing that Baldwin SPDAs were completely safe, high-yield investments, the Defendants were required to substantiate these performance claims.

> The record before us demonstrates that respondents employed the performance claim in advertising to inform consumers of the specific attributes of their product. In so doing, we find they represented to consumers that they had a reasonable basis for believing their claims were true. This is the impression respondents conveyed to the public. A performance claim is not a technique which can be used with impunity for ascribing specific attributes to a product based on nothing more than a guess that it will perform as represented. We find that the absence of a reasonable basis to support such claims would not only be a material fact, the knowledge of which might significantly affect consumer purchase decisions, but it would also mislead in light of the implied representation of sub-

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> stantiation. Thus, performance claims lacking a reasonable basis in fact may be found deceptive within the meaning of section 5 of the Federal Trade Commission Act.

National Dynamics Corp., 82 F.T.C. 488, 549-550 (1973), aff'd as modified, 492 F.2d 1333 (2d Cir.), cert. denied, 419 U.S. 993 (1974).

Simply put, the Defendants did not have any basis and certainly did not have an adequate basis for the unequivocal representations made to the consumers. A Baldwin SPDA, by its inherent nature, was never like "money in the bank." Baldwin

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SPDAs were not backed or "guaranteed" by the FDIC or some other entity. On the contrary, they were backed only by the dreams and aspirations of Baldwin, the former piano company. Without even examining the jerry-built Baldwin empire, it is clear that the Defendants' broad, unqualified, and unsubstantiated representations were misleading and deceptive.

Additionally, the Defendants -- some of the most sophisticated financial advisors in the country-- had reason to believe from the outset that Baldwin SPDAs were not risk-free, high-yield investments. From the beginning, the Baldwin Insurance Companies' financial records made clear that they were paying out more in credited interest, commissions

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and other expenses than they were collecting in SPDA premiums. Indeed, Milliman & Robertson warned from the outset that the Baldwin SPDA program was contingent upon a novel and complicated tax strategy that was subject to IRS disapproval. Also, as described in greater detail above, Baldwin's financial reports made clear that moneys generated by Baldwin SPDA sales were not invested prudently, but rather were being used to finance Baldwin's insatiable appetite for growth. Numerous commentators warned the Defendants both publicly and privately that Baldwin's acquisition strategy threatened the solvency of the Baldwin Insurance Company. In light of this knowledge, the Defendants' representations to consumers that Baldwin SPDAs

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that the act or practice had the capacity to deceive a "substantial" number of consumes. See Benrus Watch Co., Inc. v. FTC, 357 F.2d 313, 319-320 (8th Cir. 1965); cert denied, 384 U.S. 939 (1966); Raymond Lee Organization, Inc., 92 F.T.C. 489, 649 (1978), aff'd, 679 F.2d 905 (D.C. Cir. 1980); Kroger Co., 98 F.T.C. 639, 728 (1981), modified on other grounds, 100 F.T.C. 573 (1982). The deceptive act or practice need not mislead all -- or even most -- consumers to be deceptive. See, e.g., Firestone Tire & Rubber Co. v. FTC, 481 F.2d

were safe, secure investments were patently misleading and deceptive. 14/

b. The Defendants' Acts or Practices Misled or Deceived A Substantial Number of Consumers.

The second element of a deceptive trade practice is the demonstration

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14/ The Defendants cannot escape this conclusion by asserting that their sales materials were based on information given to them by Baldwin or Planco because "[t]he duty of reasonable care is not satisifed by blind reliance upon representations of others." People v. Forest E. Olson, Inc., 137, Cal.App.3d 137, 139, 186 Cal.Rptr. 804, 806 (1982) (citation omitted). Certainly the information provided to the Defendants was not so disinterested or verifiable as to constitute "such information as would satisfy reasonable and prudent businessman, acting in good faith that such representation was true." Universe Co., 63 F.T.C. 1282, 1294 (1963), aff'd sub nom. Kirschner v. FTC, 337 F.2d 757 (9th Cir. 1964).

at 249 (10% of the consumers); Bristol-Myers Co., 85 F.T.C. 688, 744 (between 14% and 33% of the consumers).

In this regard, it is important to recall who purchased the Baldwin SPDAs. According to the Defendants' market research and the States' investigations, most Baldwin SPDA purchasers were over the age of 45 who had little prior experience in investments and were seeking safe investments to provide retirement income. Thus, the Defendants' representations must be examined in light of the lack of sophisticiation and understanding of the group to whom they were directed. Raymond Lee Organization, 92 F.T.C. at 628. Particularly where, as here, consumers could not verify or even evaluate the Defendants' representa-

tions concerning safety and yield, it is prcper to conclue that a substantial number of them were misled or deceived by the Defendants' misrepresentations. See, e.g., American Home Products Corp. v. FTC, 695 F.2d at 698.

This self-evident conclusion is confirmed by surveys conducted by the States to determine what consumers believed about the Defendants' representations. See Bristol-Myers Co.., 85 F.T.C. at 744 (consideration of consumer surveys relevant to determine whether or not a significant number of consumers were deceived); American Home Products Corp., 98 F.T.C. at 393-94 (same); Benrus Watch Co., 64 F.T.C. at 1032, 1045 (same). These surveys confirm that many -- if

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not most -- of the people who purchased Baldwin SPDAs from the Defendants did so because they were led to believe by the Defendants -- who represented

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materiality under the state consumer protection statutes, it is unnecessary to prove that consumers actually relied upon the Defendants' representations. See, e.g., Firestone Tire & Rubber Co., 81 F.T.C. 398, 451 (1972), aff'd, 481 F.2d 246 (6th Cir.), cert. denied 414 U.S. 112 (1973) ("[I]t need not be shown that even one consumer actually relied on a particular false claim.").

STATUTORY PROVISIONS INVOLVED

Securities Exchange Act of 1934:

Section 78j. Manipulative and Deceptive Devices.

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange--
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.
>
> June 6, 1984, c. 404, Title 1, § 10, 48 Stat. 891.

Rules and Regulations of The Securities Exchange Commission

Reg. § 240.10b-5. Employment of Manipulative and Deceptive Devices.

> It shall be unlawful for any person, directly or indirectly,

by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(a) to employ any device, scheme, or artifice to defraud,

(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or

(c) to engage in any act, practice, or course of buisness which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

[Adopted in Release No. 34-3230, May 21, 1942, 13 F.R. 8177]

Federal Rules of Civil Procedure

Rule 1. Scope of the Rules:

These rules govern the procedure in the United States district courts in all suits of a civil nature whether cognizable as cases at law or in equity or in admiralty, with the exceptions stated in Rule 81. They

shall be construed to secure the just, speedy, and inexpensive determination of every action.

Federal Rules of Civil Procedure:

Rule 8. General Rules of Pleading:

(a) CLAIMS FOR RELIEF. A pleading which sets forth a claim for relief, whether an original claim, counterclaim, cross-claim, or third-party claim, shall contain (1) a short and plain statement of the grounds upon which the court's jurisdiction depends, unless the court already has jurisdiction and the claim needs no new grounds of jurisdiction to support it, (2) a short and plain statement of the claim showing that the pleader is entitled to relief, and (3) a demand for judgment for the relief to which he deems himself entitled. Relief in the alternative or of several different types may be demanded.

Federal Rules of Civil Procedure

Rule 9. Pleading Special Matters:

(b) FRAUD, MISTAKE, CONDITION OF THE MIND. In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally.

Federal Rules of Civil Procedure

Rule 12. Defenses and Objections -- When and How Presented -- By Pleading or Motion -- Motion for Judgment on the Pleadings:

(b) HOW PRESENTED. Every defense, in law or fact, to a claim for relief in any pleading, whether a claim, counterclaim, cross-claim, or third-party claim, shall be asserted in the responsive pleading thereto if one is required, except that the following defenses may at the option of the pleader be made by motion: ... (6) failure to state a claim upon which relief can be granted, ...

(e) MOTION FOR MORE DEFINITE STATEMENT. If a pleading to which a responsive pleading is permitted is so vague or ambiguous that a party cannot reasonably be required tc frame a responsive pleading, he may move for a more definite statement before interposing his responsive pleading....

Federal Rules of Civil Procedure

Rule 16. Pretrial Conferences; Scheduling; Management:

(a) PRETRIAL CONFERENCES; OBJECTIVES. In any action, the court may in its discretion direct the attorneys for the parties and any unrepresented

parties to appear before it for a conference or conferences before trial for such purposes as

(1) expediting the disposition of the action;

(2) establishing early and continuing control so that the case will not be protracted because of lack of management;

(3) discouraging wasteful pretrial activities;

(4) improving the quality of the trial through more thorough preparation, and;

(5) facilitating the settlement of the case.

Federal Rules of Civil Procedure

Rule 26. General Provisions Governing Discovery:

(b) DISCOVERY SCOPE AND LIMITS. Unless otherwise limited by order of the court in accordance with these rules, the scope of discovery is as follows:

(1) In General. Parties may obtain discovery regarding any matter, not privileged, which is relevant to the subject matter involved in the pending action, whether it relates to the claim

or defense of the party seeking discovery or to the claim or defense of any other party, including the existence, description, nature, custody, condition and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of any discoverable matter. It is not ground for objection that the information sought will be inadmissible at the trial if the information sought appears reasonably calculated to lead to the discovery of admissible evidence.

Federal Rules of Civil Procedure

Rule 56. Summary Judgment:

(b) FOR DEFENDING PARTY. A party against whom a claim, counterclaim, or cross-claim is asserted or a declaratory judgment is sought, may, at any time, move with or without supporting affidavits for a summary judgment in this favor as to all or any part thereof.

(c) MOTION AND PROCEEDINGS THEREON. The motion shall be served at least 10 days before the time fixed for the hearing. The adverse party prior to the day of hearing may serve opposing affidavits. The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on

file, together with the affidavits, if any, show that t there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. A summary judgment, interlocutory in character, may be rendered on the issue of liability alone although there is a genuine issue as to the amount of damages.

(e) FORM OF AFFIDAVITS; FURTHER TESTIMONY; DEFENSE REQUIRED. Supporting and opposing affidavits shall be made on personal knowledge, shall set forth such facts as would be admissible in evidence, and shall show affirmatively that the affiant is competent to testify to the matters stated therein. Sworn or certified copies of all papers or parts thereof referred to in an affidavit shall be attached thereto or served therewith. The court may permit affidavits to be supplemented or opposed by depositions, answers to interrogatories, or further affidavits. When a motion for summary judgment is made and supported as provided in this rule, an adverse party may not rest upon the mere allegations or denials of his pleading, but his response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial. If he does not so respond, summary judgment, if

appropriate, shall be entered against him.

Federal Rules of Civil Procedure

Rule 60. Relief from Judgment or Order:

(b) MISTAKES; INADVERTENCE; EXCUSABLE NEGLECT; NEWLY DISCOVERED EVIDENCE; FRAUD; ETC. On motion and upon such terms as are just, the court may relieve a party or his legal representative from a final judgment, order, or proceeding for the following reasons: (1) mistake, inadvertence, surprise, or excusable neglect; (2) newly discovered evidence which by due diligence could not have been discovered in time to move for a new trial under Rule 59(b); ....

The Rules Enabling Act

28 U.S.C. § 2072:

The Supreme Court shall have the power to prescribe by general rules, the forms of process, writs, pleadings, motions and the practice and procedure of the district courts of appeals of the United States in civil actions, ...

Such rules shall not abridge, enlarge or modify any substantive right and shall preserve the right of trial by jury as at common law and as declared

by the Seventh Amendment to
the Constitution.

Office Supreme Court
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CLERK

No. 85-36

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

MICHAEL CEASAR,

Petitioner,

—against—

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION

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BRIEF IN OPPOSITION

PRELIMINARY STATEMENT

Petitioner is a purchaser of the stock of Merrill Lynch & Co., Inc. His attempt to conjure up a securities fraud claim by repackaging unrelated *other* complaints against respondents ("Merrill Lynch") was rejected by the courts below after petitioner was afforded ample opportunity to present all materials claimed to support his allegations. Those materials established that he had no claim at all.

The courts below merely applied well-settled legal principles in reaching their conclusion. The court of appeals found the issue so clear that it affirmed unanimously by a three paragraph statement that does not constitute a formal opinion and

may not be officially reported or even cited in unrelated cases. Plainly, this case raises no significant issues, and the decisions below have no broad-ranging effect. Simply stated, there are no "special and important reasons" for granting a writ of certiorari in this action. Sup. Ct. Rule 17.

COUNTERSTATEMENT OF QUESTION PRESENTED

Was a grant of summary judgment proper where the undisputed record showed (a) that the misrepresentations alleged were in fact accurate when made and that the matters allegedly omitted would at most have been unwarranted predictions, impossible to make at the time and uncertain even now; and (b) that petitioner did not purchase in reliance on market conditions, which, in any event, were not artificially inflated as he alleged?

COUNTERSTATEMENT OF THE CASE

Petitioner, a purchaser of Merrill Lynch stock, brought this purported securities fraud action alleging that respondents had artificially inflated the market in which he purchased by making misrepresentations and omissions in certain Merrill Lynch quarterly reports. He claimed that the misrepresentations and omissions concerned Merrill Lynch's purported liability to purchasers of insurance products known as single premium deferred annuities ("SPDAs") issued by a subsidiary of Baldwin-United Corporation ("Baldwin") and sold through Merrill Lynch affiliates, as well as other problems resulting in Baldwin's financial collapse. Converting respondent's challenge to petitioner's pleading into one for summary judgment, the district court invited petitioner to come forward with any materials by which he could show a genuine factual issue to support his claim.

The materials petitioner offered, however, demonstrated that the alleged misrepresentations were not misrepresentations at

all; that the alleged omissions were, at best, mere predictions of events concerning an unrelated company outside the control of Merrill Lynch; that the events he claimed Merrill Lynch should have predicted in April 1983 are uncertain to occur even now; and that in purchasing his stock in the first instance, petitioner did not rely on artificially inflated market conditions at all, but rather believed that the market for Merrill Lynch stock was "undervalued."

On the undisputed record, the district court concluded, and the court of appeals agreed, that petitioner's claim was no more than a classic instance of "fraud by hindsight," and that, consequently, the enormous expenditure entailed in the discovery "fishing expedition" that petitioner had requested was not justified. Summary judgment accordingly was granted for respondents.

In order to clarify the context and basis of petitioner's suit, which the instant petition for certiorari distorts, a brief summary of the background and procedural posture of the action follows.

(a) Background

Petitioner purchased Merrill Lynch stock on three separate occasions from July to September, 1983 (A-30), the last at a time he believed Merrill Lynch stock to be "undervalued." During that period, the market in Merrill Lynch stock was declining consistently and rapidly; petitioner's third purchase was made at a price drop of 30% from that of his first.

The decline in Merrill Lynch stock paralleled a decline in the price of securities of other nationwide brokerage companies. According to petitioner's own securities expert, it reflected the market's reaction to the news that Baldwin and its insurance subsidiaries were suffering financial difficulties, resulting in the July 1983 commencement of rehabilitation proceedings against Baldwin's insurance subsidiaries, Baldwin's September 1983 entry into reorganization proceedings, and the consequent

filing of suits by SPDA holders against Merrill Lynch and other brokers.

In January 1984, Merrill Lynch announced that it had set aside a reserve fund of approximately $154 million, approximately 40% of which covered the obligations owed Merrill Lynch by Baldwin (A-65-66), and approximately $88 million of which was in connection with, *inter alia*, Merrill Lynch's simultaneously-announced proposal to enhance the provisions of the rehabilitation plan for the Baldwin insurance subsidiaries, thereby helping its customers who were SPDA purchasers even though it had no legal obligation to do so (A-66). To this day, Merrill Lynch has not been found liable in any way to SPDA holders whose contract rights continue to be protected by the rehabilitation plan for the Baldwin insurance subsidiaries.

Nevertheless, petitioner attempted to reshape the assertions made in the SPDA holder suits into a claim of his own. He charged that respondents had made misstatements concerning Baldwin's financial problems and respondents' liability to SPDA holders in an April 1983 statement by Roger Birk, Merrill Lynch's then-Chairman, that "Merrill Lynch was 'prepared to live and thrive whatever the rules [governing the financial business]' " (A-58) and in Merrill Lynch's 1983 First and Second Quarter Reports. The latter, he claimed, reported broad based strength in most areas of Merrill Lynch's business without qualification in the annuity area (A-58-62).

As reported in both the *Wall Street Journal* and in Merrill Lynch's 1983 First Quarter Report, the "live and thrive" statement by Roger Birk had absolutely no relevance to petitioner's claim. It was part of a lengthy speech addressed solely to the increasing competition in the financial services area as a result of commercial banks entering the securities business, to pending legislation that would further increase that competition, and to Merrill Lynch's strategy to succeed in that environment. The statements of earnings in the First and Second Quarter Reports likewise failed to support petitioner's claim.

They specifically noted a substantial decline in Merrill Lynch's annuity sales during the relevant quarters, just a few paragraphs below the language cited by petitioner (A-58-62). Indeed, the record is devoid of any evidence suggesting that the statements were inaccurate in any respect.

Petitioner also contended that Merrill Lynch knew but fraudulently failed to disclose in those quarterly reports that Baldwin SPDA holders would lose their contract rights, that Merrill Lynch ultimately would be held liable to Baldwin SPDA holders, and that Baldwin's own financial status would adversely impact Merrill Lynch because Baldwin could not repay obligations incurred in connection with its 1981 purchase of a Merrill Lynch company (A-62-63). The extent to which any of those events may occur, however, is unclear even today and their prediction two years ago not only would have been impossible but irresponsible.

(b) Proceedings Below

On April 20, 1984, Merrill Lynch moved to dismiss petitioner's complaint pursuant to Rules 9(b) and 12(b)(6) of the Federal Rules of Civil Procedure for failure to state a claim and to plead fraud with the requisite particularity. By order dated July 27, 1984, the district court stated its intention to treat the motion as one for summary judgment and established a schedule to give "all parties reasonable opportunity to present all material made pertinent to such a motion by Rule 56" (A-1-3).

After petitioner filed an Amended Complaint on August 15, 1984 (A-24-72) in an attempt to moot respondents' motion, he served a broad-ranging document request and deposition notice. By order dated September 20, 1984, the requested discovery was stayed pending disposition of the motion, with the court "reserv[ing] the right to permit discovery in the future if, after plaintiff has submitted papers opposing the motion, such discovery should appear appropriate" (A-4-5).

By Memorandum and Order dated October 10, 1984, the district court granted summary judgment for respondents and dismissed the action (A-6-8). On November 9, 1984, it denied petitioner's motion for "reargument or reconsideration and clarification" and reaffirmed its October 10, 1984 order:

> Upon examining all papers submitted, we find that the motion for summary judgment should be granted. This is essentially an action for "fraud by hindsight". The papers submitted do not suggest any reasonable basis for believing that defendants made material misstatements or omissions of fact concerning Merrill Lynch's financial prospects with knowledge or reckless disregard of the possibility that such would be misleading. To permit plaintiff to engage in discovery would be to permit a "fishing expedition" at enormous expense to the defendants.

(A-13).

The Second Circuit unanimously affirmed following its "careful review of the documentary evidence adduced below" (A-21). That court agreed both with the district court's characterization of petitioner's claim as one for "fraud by hindsight" (A-21-22), and its conclusion that no material issues of fact were raised by the record: "[e]ven assuming all factual questions were resolved in Ceasar's favor, we do not believe his claim was viable" (A-22). The court of appeals also agreed that petitioner was not entitled to discovery because his "conclusory allegations did not exceed [the] minimum standard" necessary to make out a *prima facie* claim (A-22-23).

REASONS FOR DENYING CERTIORARI

I.

ISSUES CONCERNING RULE 9(b) ARE IRRELEVANT TO THE DECISION BELOW

The principal reasons supporting the petition for certiorari concern purported distinctions in language used by the various circuits in applying Rule 9(b) of the Federal Rules of Civil Procedure (Petition at 23-40). Whether or not such subtle differences constitute a "split of authority" is certainly far from clear.[1] What is evident, however, is that neither the construction nor application of Rule 9(b) is now relevant to this action.

Although respondents originally moved against petitioner's complaint on grounds, *inter alia*, of noncompliance with Rule 9(b), the district court converted that motion into one for summary judgment (A-1-3), recognizing that it was

> based in part upon Rule 12(b)(6), dealing with the defense of failure to state a claim upon which relief can be granted. Since the parties have presented matters outside the pleadings, we will, pursuant to Rule 12(b), treat this as a motion for summary judgment under Rule 56, and give

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1 Contrary to petitioner's suggestion (Petition at 24-25), the decision of the United States Court of Appeals for the Second Circuit in *Denny* v. *Barber*, 576 F.2d 465 (2d Cir. 1978) has been recognized by numerous courts in other circuits as a leading case on the general pleading requirements and policies under Rule (9)b. *See e.g.*, *Peoria Union Stock Yards Co. Retirement Plan* v. *Penn Mutual Life Insurance Co.*, 698 F.2d 320, 324 (7th Cir. 1983); *Blanes* v. *Paine Webber Jackson & Curtis, Inc.*, 593 F. Supp. 458, 461 (D.P.R. 1983); *In re Ramada Inns Securities Litigation*, 550 F. Supp. 1127, 1132 (D. Del. 1982); *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Del Valle*, 528 F. Supp. 147, 149 (S.D. Fla. 1981); *McFarland* v. *Memorex Corp.*, 493 F. Supp. 631, 656 (N.D. Cal. 1980); *Shapiro* v. *Miami Oil Producers, Inc.*, 84 F.R.D. 234, 236 (D. Mass. 1979).

> all parties reasonable opportunity to present all material made pertinent to such a motion by Rule 56.

(A-2).

After petitioner filed his amended complaint, respondents moved against that pleading pursuant to the above order. The parties subsequently introduced hundreds of pages of exhibits and several affidavits. Both courts below reviewed and considered all of the extra-pleaded submissions, as is proper on a summary judgment motion, and did not limit themselves to the allegations in the complaint (A-13, 21). They then applied basic and well-settled legal principles in ruling that petitioner had failed to raise a genuine factual issue and that his claim was invalid as a matter of law (A-12-13, 21-22). See Point II, *infra*. Their rulings did not address the sufficiency of the pleading under Rule 9(b) in that it was no longer an issue.

Accordingly, petitioner's request that this Court determine, in the abstract, whether a split of authority among the circuits exists as to Rule 9(b) and the proper standards governing that rule's construction would be a needless expenditure of this Court's resources. The courts below simply did not decide this case on that basis. The petition for a writ of certiorari should be denied.

II.

THE COURT BELOW APPLIED WELL-ESTABLISHED LEGAL PRINCIPLES IN CONCLUDING THAT PETITIONERS HAD NO CLAIM FOR SECURITIES FRAUD

Petitioner does not point to a single unique or important issue that was resolved below, let alone one that would justify this Court's attention. As shown, he merely challenges the lower courts' application of well-established legal principles in ruling in favor of respondents.[2]

As this Court has recognized, when a party opposes a motion for summary judgment, at the very least "sufficient evidence supporting the claimed factual dispute [must] be shown to require a jury or judge to resolve the parties' differing versions of the truth at trial." *First National Bank* v. *Cities Service Co.*, 391 U.S. 253, 289 (1968). *See also* Fed. R. Civ. P. 56(e). In determining the sufficiency of that evidence, moreover, the record is to be reviewed in the light most favorable to the party opposing the motion (A-21-22). 6 J. Moore, W. Taggart & J. Wicker, *Moore's Federal Practice* ¶ 56.15[3] at 56-469 (2d ed. 1985). The courts below did nothing more than properly apply these settled principles. Contrary to petitioner's contention that the court below wrongfully drew inferences from the evidence in ruling for respondents (Petition at 42), the court specifically found that even if "all factual questions were resolved in Ceasar's favor," his claim was not viable (A-22).

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2 Petitioner's references (Petition at 41, 43) to this Court's decision in *Hishon* v. *King & Spalding*, 104 S. Ct. 2229, 2233 (1984) are inapposite. That case set forth the standard to be applied in reviewing motions to dismiss based solely on the pleadings. Here, however, evidence was offered by plaintiff supplementing and contradicting the allegations in the amended complaint; thus, those allegations were no longer the guideline for whether a genuine issue of material fact existed. *First National Bank* v. *Cities Service Co.*, 391 U.S. 253, 288-89 (1968).

Petitioner's claim was based on Merrill Lynch's alleged failure publicly to predict in April 1983 that it ultimately would be liable to holders of SPDAs issued by Baldwin subsidiaries and that Baldwin's own financial status would adversely impact Merrill Lynch as one of its creditors. Those predictions would have been impossible then and are unclear even now, two years later.

In view of this, the Second Circuit properly agreed with the district court that petitioner's claim was merely one for "fraud by hindsight," which the Second Circuit had previously held was not actionable in federal securities fraud. *Denny* v. *Barber*, 576 F.2d 465, 470 (2d Cir. 1978). In that case, the Second Circuit had noted:

> there . . . must be more than vague allegations that, as shown by subsequent developments, the corporation's true financial picture was not so bright in some respects as its annual reports had painted and that the defendants knew, or were reckless in failing to know, this.

Id. Petitioner has cited no case which rejected the holding in *Denny* v. *Barber, supra*, and our research likewise has uncovered no such decision.

Moreover, the record below negated the existence of a securities fraud claim on other grounds as well. The 1983 financial reports and statement of Merrill Lynch's then-chairman contained no "prophecy" of Merrill Lynch's future profits or earnings; they did not relate to future events in that respect at all. Nor was the market in Merrill Lynch stock during the period in issue artificially inflated. Petitioner's own expert acknowledged the decline in the price of Merrill Lynch stock and attributed it, not to the suppression of information regarding Baldwin's financial difficulties and their effect on Merrill Lynch, but rather to public awareness of precisely these events.

In view of the record, and petitioner's failure to come forward with any support for a claim *prima facie*, the court's further decision below to refuse to permit petitioner broad-ranging discovery was plainly correct. This Court has admonished that to the extent discovery

> permits a plaintiff with a largely groundless claim to simply take up the time of a number of other people, with the right to do so representing an *in terrorem* increment of the settlement value, rather than a reasonably founded hope that the process will reveal relevant evidence, it is a social cost rather than a benefit.

Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 723, 741 (1975). Such was the case here.

CONCLUSION

For the reasons set forth above and in the decisions below, the Petition for Writ of Certiorari should be denied.

Dated: July 29, 1985

Respectfully submitted,

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No. 85-36

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

MICHAEL CEASAR,

Petitioner,

– against –

MERRILL LYNCH & CO., INC., ROGER E. BIRK, DAKIN B. FERRIS and WILLIAM A. SCHREYER,

Respondents.

REPLY BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

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REPLY BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

PRELIMINARY STATEMENT

This brief addresses issues first raised by respondents in their Brief in Opposition ("Opp. Br."). Respondents contend that petitioner suffered no damages due to his reliance on the

integrity of the market for Merrill Lynch & Co., Inc. ("Merrill Lynch") stock. In fact, the price of said stock was artificially inflated due to the wrongs alleged in the complaint, as supported by the affidavits and exhibits submitted below.

QUESTION RAISED BY RESPONDENTS IN THEIR BRIEF IN OPPOSITION

Was petitioner damaged by his reliance on the integrity of the market, where, in fact, Merrill Lynch stock was artificially inflated by respondents' fraudulent conduct?

ARGUMENT

I. Petitioner Suffered Damages As A Result Of His Purchases Of Merrill Lynch Stock, Caused By Respondents' Failure To Disclose Merrill Lynch's Liability To Baldwin-United SPDA Purchasers

Respondents attempt to lead the Court to believe that petitioner was not damaged

by the wrongs pleaded in the complaint. At Opp. Br. page 3, it is stated "that in purchasing his stock in the first instance, petitioner did not rely on artificially inflated market conditions at all, but rather believed that the market for Merrill Lynch stock was 'undervalued'." On the same page, however, they concede that there was a drop in the quoted price of Merrill Lynch stock following petitioner's first purchase and that at the time of his third purchase, the price had dropped approximately 30% from the time of his first purchase.

Respondents then go on to state: "According to petitioner's own securities expert, it [the drop in the price of Merrill Lynch securities] reflected the market's reaction to the news that Baldwin and its insurance subsidiaries

were suffering financial difficulties . . . ."

Respondents overlook the fact that petitioner's damage expert, John Hammerslough, submitted an affidavit in which he stated:

> 5. The results of this comparison indicate that Merrill Lynch was the worst performing stock of those compared during the class period; during August 31-September 27 when Baldwin's financial condition further deteriorated, culminating in its bankruptcy, and the Factor litigation was anticipated and finally brought; and finally during the day of September 27, when the market was first informed of the Factor suit and the Baldwin bankruptcy filing. In every case, Merrill Lynch was the worst performing stock.

The Hammerslough affidavit, submitted below, contained a table for the period April 25, 1983-September 27, 1983 which disclosed Merrill Lynch's stock in that period to be the worst performing of the brokerage house stocks compared. Table

2 of the Hammerslough affidavit disclosed that Merrill Lynch stock, between August 31, 1983 and September 27, 1983, suffered the worst losses of those compared. Table 3 again disclosed that Merrill Lynch stock was the worst performing of those compared during the period September 26-September 27, 1983. As quoted above, the market was first informed of the Factor suit on September 27th, causing Merrill Lynch stock to fall precipitately (A-68), clearly refuting respondents' contention that petitioner was not damaged by the wrongs alleged in the complaint.

Petitioner has submitted evidence that he was damaged. Respondents disagree with petitioner's expert. This dispute as to damages should not be disposed of on a motion for summary judgment. See, Burns v. Paddock, 503 F.2d 18, 24-25 (7th Cir. 1974). Based

upon Conley v. Gibson, 335 U.S. 41 (1957), this writ of certiorari should issue, affording petitioner the opportunity to prove his damages resulting from the wrongs alleged in the complaint.

II. In Making His Purchases, Petitioner Relied on The Integrity of the Market For Merrill Lynch Shares

Respondent's contention that petitioner did not rely on artificially inflated market conditions at all (Opp. Br., p. 3) is ludicrous in the face of petitioner's affidavit submitted below in which he clearly stated that he was aware of Merrill Lynch's announced record second quarter and first half earnings and that he never would have purchased his Merrill Lynch stock had he known of the huge Merrill Lynch exposure in connection with Baldwin-United Corporation ("Baldwin"). The true value of Merrill Lynch stock would have been

reflected only if Merrill Lynch had disclosed its Baldwin liabilities. Both on the date the Factor suit was commenced and four months later when Merrill Lynch materially restated prior earnings, the stock price fell substantially on the New York Stock Exchange.

CONCLUSION

To what degree Merrill Lynch's stock was inflated by its failure to disclose its immediate pending liability in the Baldwin situation and to what extent petitioner has been damaged is a battle that should be left to the experts and the jury at trial.

Respectfully submitted,

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August 28, 1985